CHINA –MEASURES AFFECTING TRADING RIGHTS AND DISTRIBUTION SERVICES FOR CERTAIN PUBLICATIONS AND AUDIOVISUAL ENTERTAINMENT PRODUCTS

(WT/DS363)

COMMENTS OF THE UNITED STATES OF AMERICA ON CHINA'S ANSWERS TO THE SECOND SET OF QUESTIONS BY THE PANEL TO THE PARTIES

October 22, 2008

TABLE OF REPORTS

Short Form	Full Citation
EC – Bananas (Panel)	Panel Report, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/R, adopted 25 September 1997, as modified by the Appellate Body Report, WT/DS27/AB/R
EC – Bananas III (AB)	Appellate Body Report, *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, adopted 25 September 1997
Korea – Beef (AB)	Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R, WT/DS169/AB/R, adopted 10 January 2001
Mexico – Rice (AB)	Appellate Body Report, *Mexico – Definitive Anti-Dumping Measures on Beef and Rice; Complaint with Respect to Rice*, WT/DS295/AB/R, adopted 20 December 2005
Mexico – Soft Drinks (Panel)	Panel Report, *Mexico – Tax Measures on Soft Drinks and Other Beverages*, WT/DS308/R, adopted 24 March 2006, as modified by the Appellate Body Report, WT/DS308/AB/R
US – German Steel (AB)	Appellate Body Report, *United States – Countervailing Duties on Certain Corrosion-Resistant Carbon Steel Flat Products from Germany*, WT/DS213/AB/R, adopted 19 December 2002

PRELIMINARY ISSUES

Questions to China

147. *In reference to paras. 218-219 of the US second written submission and Exhibit US-62, please respond to the US argument that the Several Opinions, the Importation Procedure, and the Sub-Distribution Procedure are "legally binding on their issuing agencies, guide the enforcement of law and implementation of administrative measures and serve as a basis for particular administrative acts".

1. In its response to Question 147, China fails to rebut the U.S. argument that the Several Opinions, the Importation Procedure, and the Sub-Distribution Procedure are "legally binding on their issuing agencies, guide the enforcement of law and implementation of administrative measures and serve as a basis for particular administrative acts". China merely asserts, without any support, that the Several Opinions and the Importation Procedure are not "regulatory documents".[1] Notably, China does not contest that the Several Opinions, Importation Procedure and Sub-Distribution Procedure are legally binding. In fact, China provides no argument with respect to Exhibit US-62 in which China's Supreme People's Court describes the legally binding status of such "other regulatory documents". Moreover, China remains silent with respect to the other evidence submitted by the United States that demonstrates the legally binding status of these three documents, including the Administrative Licensing Law addressed in the U.S. response to Panel Question 4.[2]

2. China's discussion regarding the Sub-Distribution Procedure is also lacking. While the Sub-Distribution Procedure and the Network Music Opinions both implement the same decision of the State Council,[3] which is the highest organ of the Executive Branch, China asserts that only the Network Opinions, and not the Sub-Distribution Procedure, is a legal instrument. However, both measures use legally binding language, such as "shall", and contain requirements that cannot be ignored.

3. Moreover, China erroneously contends that the Sub-Distribution Procedure is only a summary of other regulations. Although the Sub-Distribution Procedure may contain provisions that are similar in some respects to other Chinese measures,[4] this does not mean that the Sub-Distribution Procedure is not a measure subject to challenge under WTO dispute settlement

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[1] It is unclear why China does not address U.S. arguments as to why the Sub-Distribution Procedure is also an "other regulatory document". *See* U.S. Answers to the First Set of Panel Questions, paras. 12-17.

[2] U.S. Answers to the First Set of Panel Questions, paras. 12-17.

[3] *See* Sub-Distribution Procedure, "Stated Basis" (Exhibit US-29); and Network Music Opinions, *Preamble* (Exhibit US-34).

[4] In fact, numerous Chinese measures at issue in this dispute contain overlapping provisions with respect to the same products and the same activities. For example, the Network Music Opinions contains content review provisions for sound recordings that are nearly identical to those contained in the Internet Culture Rule, the Audiovisual Regulation and the Audiovisual Import Rule. *See* Network Music Opinions, Article III.9 (Exhibit US-34); Internet Culture Rule, Article 16 (Exhibit US-32); Audiovisual Regulation, Article 28 (Exhibit US-16); and Audiovisual Import Rule, Article 11 (Exhibit US-17).

procedures. As the United States has explained, the Sub-Distribution Procedure is a measure,[5] and GAPP is no less bound by requirements pertaining to pre-establishment legal compliance, registered capital and operating term in the Sub-Distribution Procedure, than it is bound by similar provisions in the Foreign-Invested Sub-Distribution Rule.

4. Finally, China has still not identified the basis on which it is objecting to the Several Opinions, the Importation Procedure and the Sub-Distribution Procedure. These measures are identified in the U.S. panel request and China has not challenged their inclusion in the Panel's terms of reference. Moreover, the United States has demonstrated that these instruments are "measures" within the meaning of Article 3.3 of the DSU.[6]

148. *Please respond to the US reply to Panel Question 120 in which it argues that, pursuant to the Appellate Body ruling in *Mexico - Anti-Dumping Measures on Rice*, the US claim on reading materials under Article III:4 of the GATT 1994 is properly before the Panel.

5. China's interpretation of the Appellate Body report in *Mexico – Rice* is unreasonably narrow and does not succeed in countering the U.S. argument regarding the inclusion of its claim under Article III:4 of the GATT 1994 on reading materials in the Panel's terms of reference.[7] Under China's reading, which adopts the same "rigid approach" the Appellate Body warned against,[8] panel requests would be prevented from fully benefitting from the "exchange of information necessary to refine the contours of a dispute."[9] At no time does China address this core aspect of the Appellate Body's reasoning. Rather, China focuses its argument on limiting that reasoning to the point of irrelevance.

6. First, the Appellate Body explicitly endorsed the possibility of a "reformulation of the complaint that takes into account new information such that additional provisions of the covered agreements become relevant."[10] As the United States has demonstrated, this is precisely what occurred in the present dispute.[11] During consultations, the United States and China held extensive discussions regarding China's distribution services regime for reading materials, which resulted in the United States gaining a better understanding of the measures at issue, including

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[5] U.S. Answers to the Second Set of Panel Questions, paras. 1-9.

[6] U.S. Answers to the Second Set of Panel Questions, paras. 1-9.

[7] U.S. First Oral Statement, paras. 99-100; U.S. Answers to the First Set of Panel Questions, paras. 198-199; U.S. Second Oral Statement, para. 82; and U.S. Answers to the Second Set of Panel Questions, paras. 23-29.

[8] *Mexico – Rice (AB)*, para. 136.

[9] *Mexico – Rice (AB)*, para. 138.

[10] *Mexico – Rice (AB)*, para. 138.

[11] U.S. First Oral Statement, paras. 99-100; U.S. Answers to the First Set of Panel Questions, paras. 198-199; and U.S. Answers to the Second Set of Panel Questions, paras. 23-29.

information that revealed related national treatment concerns regarding the reading materials that foreign distributors are prohibited from distributing.

7. Second, China incorrectly asserts that the U.S. claim under Article III:4 of the GATT 1994 does not evolve out of the U.S. claims under the GATS and China's trading rights commitments. A GATT 1994 claim with respect to discrimination in product distribution opportunities arising out of particular measures is a very natural evolution of a consultation addressing discriminatory distribution services opportunities created by those measures. Indeed, both claims involve the same measures, the same products, the same distributors and the same distribution channels. Moreover, the U.S. consultation request also addressed reading materials in the context of China's trading rights commitments. In other words, aspects of the consultations that addressed barriers to reading materials entering China also led to the gathering of information about the treatment of those reading materials immediately after their entry into China. This, too, contributed to the evolution of the U.S. claims regarding materials being distributed in China.

8. Finally, China's interpretation would place consultation requests above panel requests in a manner unsupported by the DSU. According to China, the scope of the claims included in a panel request would be limited to the provisions of the covered agreements included in the preceding consultation request, so that only additional sub-paragraphs of an article in a covered agreement already identified in a consultation request could be included in the subsequent panel request. Contrary to China's contention, it is the panel request, rather than the consultation request, that establishes a panel's terms of reference.[12] Neither the text of the DSU nor the Appellate Body's reasoning in *Mexico – Rice* supports China's approach.

149. Please respond to para. 74 of the US second oral statement with respect to the panel (paras. 7.27 and 7.45) and Appellate Body (para. 140) reports in *EC - Bananas III*.

9. Question 149 addresses the U.S. argument regarding the inclusion of Film Distribution and Projection Rule, the Audiovisual Regulation and the Audiovisual Import Rule in the Panel's terms of reference and the relevance of the panel and Appellate Body reports in *EC – Bananas III* to those arguments. In order to demonstrate the flaws in China's response to Question 149, it is first necessary to identify the complete panel request at issue in *EC – Bananas III*. In that dispute, the panel and the Appellate Body found that the following panel request "contains sufficient identification of the specific measures at issue to fulfill the requirements of Article 6.2 of the DSU":[13]

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[12] *US – German Steel (AB)*, para. 124 (stating, "pursuant to Article 7 of the DSU, a panel's terms of reference are governed by the request for establishment of a panel. Article 6.2 of the DSU sets forth the requirements applicable to such requests.").

[13] *EC – Bananas III (Panel)*, para. 7.27; and *EC – Bananas III (AB)*, para. 140.

> The European Communities maintains a *regime* for the importation, sale and distribution of bananas established by Regulation 404/93 (O.J. L 47 of 25 February 1993, p. 1), and subsequent EC legislation, regulations and administrative measures, including those reflecting the provisions of the Framework Agreement on bananas, which implement, supplement and amend that *regime*.[14]

10. The panel request in *EC – Bananas III* consists of three parts: a narrative explanation of the challenged regime (*i.e.*, the EC banana regime); an explicit reference to one of the legal instrument that establishes that regime (*i.e.*, Regulation 404/93); and a clause incorporating other legal instruments that "implement, supplement and amend *that regime*". In the present dispute, the U.S. panel request contains the same tripartite structure:

> - a narrative explanation of the challenged regimes (*i.e.*, China's state-owned importation regime for imported films[15] and China's twin-track content review regime for sound recordings[16]);
>
> - an explicit reference to some of the legal instruments that establish the challenged regimes (*i.e.*, films: the Film Regulation and the Provisional Film Rule[17]; and sound recordings: the Network Music Opinions and the Internet Culture Rule[18]); and
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> - a clause incorporating "any amendments, related measures, or implementing measures" regarding those respective regimes.[19]

11. China's response to Question 149 fails to address the U.S. arguments for three reasons.[20] First, China contends that the panel and Appellate Body reports in *EC – Bananas III* establish an "explicit link" requirement, whereby measures not explicitly identified in a panel request must contain an explicit reference to a measure identified in that panel request, in order to be included in the Panel's terms of reference. However, neither the panel nor the Appellate Body articulated such a requirement.

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[14] Emphasis added.

[15] U.S. Panel Request, Section I, para. 2 (stating "[d]espite those commitments, China reserves to certain Chinese state-designated and wholly or partially state-owned enterprises the right to import the Products").

[16] U.S. Panel Request, Section IV, para. 2 (stating "China appears to require that sound recordings imported into China in physical form but intended for digital distribution must undergo content review by the Chinese Government prior to such distribution within China. However, domestically produced sound recordings appear not to be subject to this requirement, but can instead be digitally distributed immediately.").

[17] U.S. Panel Request, Section I, para. 3.

[18] U.S. Panel Request, Section IV, para. 3.

[19] U.S. Panel Request, Section I, para. 3; and U.S. Panel Request, Section IV, para. 3.

[20] U.S. First Oral Statement, para. 88; and U.S. Second Oral Statement, para. 74.

12. Rather, the panel found, and the Appellate Body affirmed, that "[w]hile the request does not identify the subsequent EC legislation, regulations and administrative measures that further refine and implement the basic regulation, we believe that the 'banana regime' that the Complainants are contesting is adequately identified."[21] Thus, the panel and Appellate Body reports in *EC – Bananas III* do not stand for the proposition for which they are cited by China. China fails, therefore, to exclude the Film Distribution and Projection Rule, the Audiovisual Regulation and the Audiovisual Import Rule from the Panel's terms of reference on the basis of a non-existent "explicit link" requirement.

13. Second, China's relies on a partial quote of the panel request in *EC – Bananas III* to argue that the Film Distribution and Projection Rule, the Audiovisual Regulation and the Audiovisual Import Rule are not within the Panel's term of reference because they are not "subsequent to" measures identified in the U.S. panel request in the present dispute. China's reliance on this incomplete excerpt is misplaced. The panel request in *EC – Bananas III* identified the measures at issue as the EC bananas regime and those instruments that establish, implement, supplement and amend *the EC banana regime*, and not simply Regulation 404/93, as China suggests. As the panel concluded, the EC banana regime was adequately identified and the instruments that establish etc. that regime, including those that were not explicitly enumerated, were properly before the panel.

14. Thus, the panel and Appellate Body in *EC – Bananas III* did not conclude that measures that establish, implement, supplement and amend the regime described in the panel request's narrative are only those issued subsequent to the measures explicitly identified in the panel request.[22] Indeed, China's argument to the contrary ignores the central finding in *EC – Bananas III*, *i.e.*, that the *regime* was adequately identified. In the present dispute, the regimes described in the panel request, including pre-existing implementing regulations covered by the scope of the narrative and related to specifically listed measures are within the Panel's terms of reference. China's argument that the Film Distribution and Projection Rule, the Audiovisual Regulation and the Audiovisual Import Rule are outside the Panel's terms of reference because they are not subsequent to the measures explicitly enumerated in the panel request is inconsistent with the reasoning in *EC – Bananas III* and should be rejected.

15. Third, China argues that the relationship between the Film Distribution and Projection Rule, the Audiovisual Regulation and the Audiovisual Import Rule and the challenged regimes for film importation and sound recording content review is irrelevant. This argument is unavailing. The panel request in *EC – Bananas III* was premised upon a relationship between the EC bananas regime and the instruments that establish, implement etc. that regime. The same

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[21] *EC – Bananas III (Panel)*, para. 7.27.

[22] Contrary to China's assertion in its response to Question 149, the Film Distribution and Projection Rule (issued December 18, 2001) was issued subsequent to the Film Regulation (issued December 12, 2001). *See* U.S. Answers to the First Set of Panel Questions, para. 7.

is true in the present dispute. The Film Distribution and Projection Rule not only implements the Film Regulation, it is also one of the principal legal instruments establishing China's state-owned film importation regime. Likewise, the Audiovisual Regulation and the Audiovisual Import Rule are two of the foundational legal instruments upon which China's twin-track content review regime for sound recordings is established.

16. As was the case with the relationship between the un-enumerated measures and the EC bananas regime in *EC – Bananas III*, the three instruments at issue are not only measures related to the respective challenged regimes (as well as the measures explicitly enumerated in the panel request), they are also measures which establish and implement the regimes in question. Contrary to China's concerns regarding burden of proof, the U.S. panel request clearly identified the challenged regimes and gave China sufficient notice regarding the inclusion of the Film Distribution and Projection Rule, the Audiovisual Regulation and the Audiovisual Import Rule as measures that amend, relate to and implement those regimes.

Question to Both Parties

150. *The Panel has preliminarily identified a variety of provisions where the Parties have provided differing translations of provisions of China's measures or dispute the meaning of particular terms which are material to resolving the dispute. These provisions are provided to the Parties, in Annex A to the Panel's Questions. Please confirm to the Panel your representations at the second substantive meeting that:

(a) The Parties will attempt to bilaterally agree on a single translation of the provisions of China's measures and provide the agreed upon translations by 9 October 2008.

(b) Also by 9 October 2008, the Parties will inform the Panel as to any provisions they cannot agree upon.

(c) Additionally, the Parties will provide the Panel, on that date, a joint suggestion as to the procedures that could be used to arrive at a single definitive translation of these provisions, should the Panel subsequently consider that this is necessary for the purpose of disposing of the claims put before the Panel.

17. On October 20, 2008, the United States and China jointly submitted a letter and mutually agreed translations of several of the measures identified by the Panel in Annex A to the second set of Panel questions. As set forth in that letter, on October 24, 2008, both the United States and China will submit their preferred translations for those measures for which the parties were not able to reach a mutually agreed translation, including each party's rationale for the preferred translation.

TRADING RIGHTS

Questions to China

168. With respect to para. 78 of China's second written submission, please provide, from the WTO agreements themselves or through the application of the rules of interpretation of customary international law, support for your contention that the right to regulate trade "is the expression of a general right of WTO Members to maintain certain measures and to pursue legitimate policy objectives".

18. In its response to Question 168, China has not – on the basis of either the WTO agreements or the customary rules of interpretation – demonstrated that the right to regulate trade "is the expression of a general right of WTO Members to maintain certain measures and to pursue legitimate policy objectives". China has established no link between the individual provisions of treaty text that it cites and the relevant provisions of its Accession Protocol. In particular, there is no basis for China's suggestions that the individual WTO provisions it cites are "expressions of a general right". In making this argument, China is simply assuming the existence of the "general right" whose existence is at issue.

19. The United States would also note that it agrees with China in general that WTO Members may pursue their national policy objectives as long as they do so in a manner consistent with the WTO Agreement. However, China's measures at issue are inconsistent with its trading rights commitments, and, without prejudice to the question of the applicability of Article XX of the GATT 1994 to those trading rights commitments, are not justified under Article XX.

169. With reference to para. 84(b) of the Working Party Report, please provide examples of actual or potential requirements concerning import licensing, TBT or SPS requirements that relate to traders rather than traded goods.

20. The United States notes that, in its response to Question 169, China does not disagree with the U.S. argument that requirements concerning import licensing, TBT and SPS relate to the goods being traded, rather than the traders of those goods. The United States submits that the "right to regulate trade" clause found in paragraph 5.1 of the Accession Protocol includes these and other requirements relating to goods being traded. While paragraph 84(b) provides that "requirements for obtaining trading rights would be for customs and fiscal purposes", that paragraph does not condition obtaining trading rights on compliance with requirements concerning import licensing, TBT and SPS. Rather, foreign enterprises and individuals with trading rights must ensure that the goods they are trading comply with such import licensing, TBT and SPS requirements. Finally, while China asserts that there must be trading rights requirements related to traders, China never explains what those alleged requirements are. As noted above, China does not argue that import licensing, TBT and SPS requirements relate to traders.

170. With reference to China's reply to Panel Question 25(b), please indicate whether Art. 5 of the Film Regulation and Arts. 3 and 16 of the Provisional Film Regulation provide for an approval process, a designation process, or both.

21. China's response to Question 170 comports with the U.S. understanding that importers of imported films are selected through China's "designation" process. China's response makes clear that the use of the term "approval" for the process provided for in Article 16 of the Provisional Film Rule is a misnomer, since this is actually a "designation process". As the United States has demonstrated, this particular "approval" process contains no application procedures or other conditions, unlike other "approval" processes provided for in this and other measures.[23]

171. Do Art. 5 of the Film Regulation and Art. 16 of the Provisional Film Rule set out approval or designation requirements?

22. China's response to Question 171 also comports with the U.S. understanding that importers of imported films are selected through China's "designation" process.

172. China's reply to Panel Question 40 suggests that the purpose of a designation system is to limit the number of importers. Please elaborate further on the purpose of such a system.

23. In its response to Question 172, China acknowledges the limiting effect of the designation system, stating that this system results in a "limited number of importers." This is confirmed by China's response to Question 40. In that answer, China explains that the designation system "ensure[s] greater efficiency and [] avoids unnecessary delays to normal trade flows", which is consistent with China's description in its first written submission of its trading rights regime – with the designation regime as its centerpiece. There, China explains, "[t]he laws and regulations at issue provide for the limitation of the total number of entities approved for engaging in the importation of cultural goods" and that these limitations are "justified []for the content review to be efficient and smooth and its impact on trade in cultural goods to be limited."[24] Moreover, China contends that its trading rights limitations satisfy the requirements of the *chapeau* of Article XX of the GATT 1994 because the "selection process is based on requirements adapted to the need to ensure an efficient content review while limiting its collateral trade effects."[25] As China has explained, these limitations are intentional and an integral part of the measures at issue in this dispute.

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[23] U.S. Answers to the First Set of Panel Questions, paras. 31-33.

[24] China's First Written Submission, paras. 215-220.

[25] China's First Written Submission, para. 232.

173. *Does the Catalogue have any independent legal effect, or is any legal effect it may have the result of the Foreign Investment Regulation, or another legal instrument?

24. China's response to Question 173 comports with the U.S. understanding that the Catalogue has independent legal effect and that it prohibits or otherwise restricts all foreign enterprises and all foreign individuals, whether or not registered in China, from engaging in various activities with respect to the products at issue.

174. With reference to Art. 42 of the Management Regulation, are foreign individuals and foreign enterprises subject to the State plan?

25. China's argument that foreign individuals and foreign enterprises are not subject to the State plan is unavailing. Article 42 provides that all applicants must satisfy at least two criteria, they must be Chinese wholly state-owned enterprises and they must conform with the State plan. It appears that, according to China, if the state-owned enterprise requirement were removed, foreign individuals and foreign enterprises would not be subject to the express State plan requirement. This, however, would be plainly inconsistent with its own law. As the United States explained in it response to Question 156, foreign individuals and foreign enterprises are subject to the State plan as Article 42 applies to *all* applicants seeking to import reading materials, AVHE products and sound recordings into China.[26] The fact that foreign individuals and foreign enterprises do not satisfy the state-ownership requirement does not relieve them from the distinct State plan requirement.

175. Do Arts. 8 and 9 of the Audiovisual Regulation apply to foreign individuals and foreign enterprises not invested or registered in China?

26. As China concedes, in response to Question 175, Articles 8 and 9 of the Audiovisual Regulation, which relate to the establishment of an audiovisual publishing entity, do not apply to foreign individuals and foreign enterprises not invested or registered in China. Specifically, China notes that foreign investors are "prohibited from investing in publishing of audiovisual products." Moreover, Article 42 of the Management Regulation also provides that only wholly State-owned entities may import unfinished audiovisual products.[27]

176. With reference to the US reply to Panel Question 5, does China agree that the term "foreign investor" encompasses foreign individuals, foreign enterprises not invested or registered in China and foreign-invested enterprises? Please explain.

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[26] U.S. Answers to the Second Set of Panel Questions, para. 39.

[27] Management Regulation, Article 42 (Exhibit US-7); *See* U.S. Answers to the Second Set of Panel Questions, paras. 40-41; *See also* U.S. First Written Submission, paras. 260-64.

27. The United States refers the Panel to Exhibit US-102 setting forth an explanation of the U.S. translation of the relevant terms. China's position that foreign-invested enterprises are not covered by Article 4 of the Several Opinions is fundamentally flawed.[28] Indeed, as the United States set forth in Exhibit US-102, the distinction that China attempts to draw between foreign individuals and foreign enterprises on the one hand and foreign-invested enterprises on the other hand is without merit.

28. Even an analysis of China's translation of the relevant terms leads to the conclusion that foreign investors – whether foreign individuals or foreign enterprises – acting through investment – are prohibited from engaging in the activities listed in Article 4 of the Several Opinions.[29]

177. *With reference to China's position on measures governing motion pictures, in its reply to Panel Question 36(b), China says that relevant measures govern the importation of motion pictures for theatrical release, not goods. On the other hand, in the same reply, China says that relevant measures govern the commercial exploitation of imported motion pictures, which consists in the supply of a series of services, including the importation of motion pictures. Furthermore, at para. 47-48 of its second written submission, China says that its measures regulate the importation of motion pictures as part of the supply of services involved in the exploitation of motion pictures for theatrical release. Finally, at para. 30 of its second oral statement, China says that its measures regarding importation of "film" relate to the content and not the physical carrier. Please explain more clearly the various statements and their relationship, as several interpretations seem possible.

In this regard, please also answer the following questions:

(a) Is China arguing that "motion pictures" as distinct from cinematographic film are services, not goods, and that an importer of motion pictures is an importer of services? If so, is the content the service, and how is "content" imported into China?

(b) Or is China arguing that importation is a service which is being regulated?

(c) What is the precise service to which cinematographic film is, in China's view, a mere accessory?

29. The United States would like to begin by noting that while China engages in a lengthy discussion of its view that there is a complete dichotomy between tangible cinematographic film and a motion picture, China, in fact, has conceded in response to Question 179 that importation

[28] Exhibit US-102, paras. 1-8; *See also* U.S. Answers to the First Set of Panel Questions, paras. 18-19.

[29] *See* Exhibit US-102, paras. 5-8.

of cinematographic film containing a motion picture can only occur via a SARFT-designated entity.[30] Accordingly, China has conceded that the relevant measures do not merely regulate motion pictures, rather than cinematographic film; in fact, the measures regulate an integrated good that consists of a carrier medium containing content.

30. In addition, in response to Question 177, China states that "[w]hen these distribution services are provided using a tangible carrier (e.g., cinematographic film), *a physical importation of this good takes place (customs clearance)*. However, this *imported good* is a mere accessory of the distribution services."[31] This is simply the latest version of China's argument that a good that is used to provide a service is not subject to goods disciplines. It is significant, however, that China concedes in the context of that very argument that the importation of a good is involved. Moreover, China has provided no legal authority supporting the proposition that a good used to provide a service is outside the scope of China's trading rights commitments.[32]

31. China's discussion of the relevant CPC classifications is also unavailing. The description of cinematographic film under Subclass 3895 of the CPC and heading 3706 of the Harmonized Commodity Description and Coding System (HS) makes clear that the hard-copy medium containing content is classified as an integrated good. These classifications do not separate the content from the good.[33]

32. Furthermore, China repeats its assertion that the measures at issue regulate the right to import motion pictures (the content) and not cinematographic film. As the United States has set forth previously, this assertion is unsupported and contradicted by other statements China has made in this dispute.[34] China provides no citations to the relevant measures – let alone any textual analysis – to support this assertion. In addition, this assertion is contradicted by China's own statement, in response to Question 179, that importation of cinematographic film containing a motion picture is restricted to SARFT-designated entities. Thus, even if China were correct that its measures only regulate the importation of content, and not importation of goods, this would not make China's measures consistent with its trading rights commitments. The measures limiting who may import motion pictures into China – assuming China is correct that the measures do not regulate hard-copy films – also limit who may import the cinematographic good containing that motion picture, as China conceded in response to Question 179.

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[30] China's Answers to the Second Set of Panel Questions, Question 179.

[31] China's Answers to the Second Set of Panel Questions, Question 177 (emphasis added).

[32] *See* U.S. First Oral Statement, paras. 9-18; U.S. Second Written Submission, paras. 18-20; U.S. Second Oral Statement, paras. 4-13.

[33] U.S. Second Oral Statement, paras. 4-8.

[34] U.S. Second Oral Statement, para. 11.

33. China also errs in its contention that the meaning of the Chinese term, "*jinkou*," supports the notion that a film for theatrical release is not a good. Article 31 of the Films Regulation sets forth the requirement that imported films are subject to "import procedures at Customs." In this context, the Chinese text of the measure uses the word "*jinkou*" to mean "import." In other words, China uses the term "*jinkou*" to refer to the import of goods subject to customs procedures. In addition, the *New Century Chinese-English Language Dictionary* defines "*jinkou*" as "import," and refers to the importation of various goods.[35] Thus, the plain meaning of "*jinkou*" and its use in the context of China's measures reinforce the conclusion that China treats imported films as goods.

178. In reference to para. 28 of the US second written submission, please comment on the treatment of HS heading 3706 as well as the CPC classifications in Subclass 3895 and 96113? In your answer can China please also address the explanatory notes to 96113.

34. As set forth above, China's discussion of the CPC and HS classifications is flawed. The fact that the CPC classifies services involving a particular good does not mean that the good is no longer a good. Indeed, the CPC classifies many services that involve the use of a particular good and separately classifies the goods themselves as goods. The services classifications do not convert all of these goods into something other than a good.

35. With respect to the specific description of the services in the relevant CPC subclasses – 96112, 96121, and 96113 – China contends that "[t]hese three categories highlight that the exploitation of motion pictures for theatrical release consists of a series of services . . .and not of trade in goods."[36] China's line of reasoning does not withstand scrutiny. Pointing out that certain services classifications related to motion pictures "highlight" that the commercial exploitation of motion pictures involves services is tautological and in no way establishes that the same services do not involve the use of goods. Moreover, China's assertion that these services descriptions focus on the content, rather than the cinematographic film, is irrelevant since the provision of these services will typically involve use of the good containing the content. The relevant goods classification in the CPC, class 3895, does not refer to cinematographic film not containing content. To the contrary, the good that is classified in CPC subclass 3895 and HS heading 3706 is an integrated good consisting of a carrier medium and content. The services provided also involve use of the carrier medium containing content.[37]

36. China maintains that the fact that HS heading 3706 describes cinematographic film as the material used "for the projection of motion pictures" confirms that the good is merely related to services. Even if this were so, China provides no support – and none exists – for the proposition

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[35] *A New Century Chinese-English Language Dictionary*, p. 823 (Exhibit US-105).

[36] China's Answers to the Second Set of Panel Questions, Question 178.

[37] *See* U.S. Second Oral Statement, para. 8.

that because a good is related to services, it is no longer a good. Moreover, the HS description of heading 3706 in fact confirms that the good involved is an integrated product consisting of the tangible carrier medium and its content that may be commercially exploited in a particular way.[38] Finally, the fact that the CPC classifications for services relating to motion pictures refer to the exploitation of the content does not mean that there is no good involved containing that content or that China's measures cannot and do not limit who can trade in that good. For example, subclass 96113 of the Provisional CPC classifies sale and rental services involving use of video tapes. The provision of this service involves commercial exploitation of a video tape, which China agrees is a good. This services classification does not transform video tapes into something other than a good.

179. Do China's arguments with respect to Articles 30 and 33 of the Regulation on Film in paras. 48 and 49 of its second written submission mean that there are no restrictions on who may import exposed and developed cinematographic film?

37. The United States notes that China concedes, in response to Question 179, that the importation of cinematographic film containing a motion picture is limited to entities designated by SARFT.

180. With reference to para. 40 of China's second written submission, where motion pictures are transmitted without any physical carrier, would the measures at issue, i.e., the Film Regulation, Provisional Film Rule, etc., be applicable in the same way as they are when it is the hard copy cinematographic film that is imported?

38. China's response to Question 180 confirms that the importation of a motion picture, regardless of the medium, is limited to entities designated by SARFT.

181. *In para. 97 of China's second written submission China states that it has explained "why this selection process is necessary in order to ensure that the content review of imported cultural goods is enforced in a manner which achieves the level of protection sought by China." At para. 100, China says that content review of imported cultural goods is, also, "necessary". Finally, in response to Panel Question 55, China said the measure to be justified as "necessary" is the restriction of the right to trade. Please clarify whether it is the selection of the importation entities or the content review which you believe is necessary to protect public morals.

39. The Appellate Body has consistently held that the party invoking Article XX of the GATT 1994 must demonstrate that the measures at issue fulfill the requirements of one of the sub-paragraphs of Article XX and that the measures must be applied in a manner that satisfies the

[38] U.S. Second Oral Statement, para. 8.

Article XX *chapeau*. The United States has shown that the measure at issue is China's failure to provide the right to trade to all foreign enterprises, all foreign individuals and all enterprises in China with respect to reading materials, AVHE products, sound recordings and films for theatrical release.[39]

40. China, however, has been inconsistent in its description of the measure at issue. While China's response to Question 181 states that it is the "selection of the importation entities" – which the United States understands as its trading rights prohibition – that is "necessary" under Article XX(a), this is not the argument China has made in the relevant parts of its submissions, including those cited in Question 181. In fact, much of China's discussion under Article XX has addressed whether its content review regime is "necessary" to protect public morals. China has failed to demonstrate that its trading rights prohibition is "necessary", in part because it has not established a nexus between its content review regime and its importation regime.

41. Finally, contrary to China's broad statement, issues regarding China's process for engaging in content review are relevant to this dispute. In response to China's argument that its trading rights prohibition is "necessary" within the meaning of Article XX(a), the United States has identified several reasonably-available WTO-consistent alternatives, each of which addresses content review. Each of these alternatives may be addressed by the Panel, for the reasons explained in the U.S. response to Question 165.[40] Separately, the United States recalls its claim under Article III:4 of the GATT 1994 regarding China's discriminatory content review system imposed on imported sound recordings intended for electronic distribution.

182. With reference to the US reply to Panel Question 1, where the United States identifies the provisions it alleges give rise to a breach of Protocol commitments, please explain how each of these provisions could be justified under Article XX(a).

42. In its response to Question 182, China is unable to explain how each of the provisions identified by the United States in Question 1 are justified under Article XX(a) of the GATT 1994. In fact, of the 12 measures identified in Question 1, China addresses only six of those measures in the context of Article XX(a).

43. First, China continues to contend that the Film Regulation, the Film Distribution and Projection Rule and the Provisional Film Rule are not subject to Article XX and has not once, even in the alternative, attempted to justify these measures under that article. While the United States takes no position on the applicability of Article XX to China's trading rights

[39] U.S. Answers to the First Set of Written Questions, paras. 93-94.

[40] U.S. Answers to the Second Set of Panel Questions, paras. 74-78.

commitments, the United States has shown that these measures govern goods[41] and that they are not justified under Article XX.[42]

44. Second, China argues that the Several Opinions and the Importation Procedure are justified under Article XX(a) because they are part of the selection regime for content review entities. As explained in the U.S. response to Question 181 above, China is once again mistaking its content review regime with the measure at issue (*i.e.*, its trading rights prohibition), while failing to explain why the latter is necessary to protect public morals. In fact, while the Several Opinions and the Importation Procedure both prohibit all foreign enterprises and all foreign individuals from importing the products at issue, neither measure even mentions content review in the context of importation.

45. Third, China describes the trading rights restrictions contained in the Management Regulation, the Catalogue, the Audiovisual Regulation and the Audiovisual Import Rule, without offering any analysis relevant to its Article XX defense. China provides no argumentation regarding whether these measures are "necessary" nor whether they "protect public morals". While China fails to even identify relevant provisions of the Management Regulation and the Catalogue, it chooses to cite Article 8 of the Audiovisual Import Rule and Article 27 of the Audiovisual Regulation. These two articles confirm that only entities "designated" at the complete discretion of the Ministry of Culture are permitted to imported finished audiovisual products (*i.e.*, AVHE products and sound recordings), but make no reference to content review.

46. Therefore, China has failed to demonstrate that its measures are justified under Article XX(a).

183. With reference to China's reply to Panel Question 42, China merely repeats that it considers all of the relevant prohibited contents to have a negative impact on public morals. Please "explain why and how", as requested by the Panel in Question 42.

47. In its responses to both Questions 42 and 183, China avoids providing an explanation of why and how the specific prohibited content enumerated in its measures has a negative impact on public morals. Moreover, China simply asserts that the attitudes, etc. reflected in *most* cultural goods reflect standards of right and wrong conduct that are not those of the importing community or nation. The United States disagrees and notes that this statement is belied by the fact that so many foreign cultural goods are in fact eventually allowed to enter China.

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[41] U.S. First Oral Statement, paras. 8-18; U.S. Answers to the First Set of Panel Questions, paras. 41-49; U.S. Second Written Submission, paras. 11-29; U.S. Second Oral Statement, paras. 4-13; and U.S. Answers to the Second Set of Panel Questions, paras. 42-45.

[42] U.S. First Oral Statement, paras. 32-39; U.S. Answers to the First Set of Panel Questions, paras. 93-94; U.S. Second Written Submission, paras. 43-57; U.S. Second Oral Statement, paras. 23-38; and U.S. Answers to the Second Set of Panel Questions, paras. 74-78.

48. Also noteworthy is China's lack of explanation of how its concerns regarding imports causing "confusion among the public as to the standards of right and wrong conduct" correspond to China's argument that reading materials in the "limited distribution category" contain prohibited content and are regularly read by government agencies and institutions.[43] China has yet to answer how this significant exception to its ban on prohibited content, which includes approximately 1,000 titles a year,[44] is consistent with its defense under Article XX of the GATT 1994.

184. For the purposes of determining the "necessity" of the challenged Chinese measures under Article XX(a) of the GATT 1994, should the Panel treat all prohibited contents that may have a negative impact on public morals in China alike, or could the challenged measures be determined to be "necessary" in relation to one type of prohibited content, but not another, e.g., on the grounds that dissemination of the one type of content would have a more serious impact on public morals than dissemination of the another type? If so, please indicate how the Panel could conduct this type of inquiry.

49. The United States recalls that as the party invoking Article XX(a) of the GATT 1994, China bears the burden of demonstrating that the measures at issue are "necessary to protect public morals" and they are applied in a manner consistent with the *chapeau* of Article XX. As explained above in response to Question 181, the measure at issue is China's trading right prohibition and not its content review regime. The United States takes note of China's position that the Panel should treat all types of prohibited content alike for purposes of this dispute.

50. Thus, the issue at hand is whether the failure to provide trading rights to all foreign enterprises, all foreign individuals and all enterprises in China is "necessary to protect public morals". China, however, has failed to show that it is necessary to prohibit trading rights to these importers in order to ensure that prohibited content does not enter the Chinese market. That gate-keeping function is provided by the content review process, which is distinct from the importation process, both conceptually and in practice.

185. *With reference to para. 143 of China's first written submission and para. 33 of the US first oral statement, where reference is made to Article 31 of the Film Regulation, is China referring to human or financial governmental resources? Also, are limited governmental resources an issue for cultural goods other than films for theatrical release, but not for films for theatrical release? If so, why? For each of the relevant products, please tell the Panel who bears the cost of conducting the content review (the Government and thus the taxpayer, the importing entity, etc.) and estimate what these costs are.

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[43] China's First Written Submission, para. 543; China's Answers to the First Set of Panel Questions, Question 130; and China's Second Oral Statement, paras. 131-134.

[44] China's First Written Submission, para. 545.

51. China's argument that cost is a factor limiting the government's ability to conduct content review does not withstand scrutiny. Despite the Panel's request, China fails to provide any information regarding who bears those costs and estimates regarding what those costs are. It is difficult to accept China's arguments regarding the prohibitive nature of content review costs, when it declines to provide the evidence that the Panel has requested.

52. Moreover, China's prohibitive cost argument is belied by the fact that the Chinese Government currently conducts the content review for AVHE products, sound recordings and films for theatrical release, and plays a central role in the content review of reading materials. MOC reviews the content for all AVHE products and sound recordings,[45] SARFT reviews the content of all imported films,[46] and GAPP reviews all titles before they are imported, is authorized to directly review the content of reading materials, and may be requested by importers to perform such review.[47] While China asserts that importers conduct "preliminary review" of films for theatrical release, AVHE products, and sound recordings, it has yet to adduce any legal authority to that end as evidence.

186. With reference to the US reply to Panel Question 21, please comment on the impact on international trade of the alternatives suggested by the United States and compare their impact to that of China's current measures. In this regard, please address whether the fact that only state-owned enterprises can import relevant products may adversely affect trade.

53. The United States notes at the outset that it has identified three reasonably available WTO-consistent alternatives to China's trading rights prohibition – content review conducted by all importers with qualified experts, content review conducted by domestic entities with appropriate expertise, and content review conducted by the Chinese Government – each of which would permit all foreign enterprises, all foreign individuals and all enterprises in China the right to import the products at issue into China.[48] China's response to Question 186, however, only addresses the first two of these alternatives and fails to discuss content review by the Chinese Government.

54. Furthermore, China's dismissal of the trade impact of these alternatives is unjustified. The three alternatives would have a profoundly positive impact on Chinese trading rights commitments, as they would permit all of the intended beneficiaries of those commitments to engage in the importation of the products at issue, while permitting China to maintain its desired level of enforcement. This would be a marked improvement on China's current trading rights

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[45] Audiovisual Regulation, Article 28 (Exhibit US-16); and Audiovisual Import Rule, Articles 11-18 (Exhibit US-17).

[46] Film Regulation, Article 31 (Exhibit US-20).

[47] Management Regulation, Article 44 (Exhibit US-7).

[48] U.S. Second Oral Statement, para. 25.

prohibition that bears no immediate relationship to preserving that desired level of enforcement. While China is correct that these alternatives would result in a "multiplication of importation entities", it is not necessarily true that this will also lead to a multiplication of content review entities, as China contends in its response to Question 186. Indeed, there would be no increase in the number of such content review entities if the Chinese Government were to continue to perform content review for AVHE products, sound recordings and films for theatrical release as it does now. Likewise, were GAPP to expand its current central role in the content review process and conduct the exclusive review of reading materials, there would be no additional content review entities.

55. China also argues that the three alternatives could lead to delays in the content review process. This suggestion is neither substantiated nor warranted. Indeed, the U.S. alternatives implement China's trading rights commitments, address China's cost/burden concerns, and preserve its desired level of enforcement.

56. Finally, China concludes that the U.S. alternatives would "not have the effect of allowing a greater volume of products to be imported into China." Beyond the unsupported nature of this assertion, in the present dispute, the United States has not argued that China's trading rights prohibition has suppressed the number of products imported into China. China cannot now argue that the U.S. alternatives fail because they do not result in a greater volume of products to be imported into China. The U.S. alternatives address the measure at issue, which is China's trading rights prohibition.

187. With reference to China's reply to Panel Question 45, please explain the relevance of paras. 4 and 5 in Exhibit CN-22 to the issue of what the "specific requirements" are.

57. Consistent with its explanation of the "selection criteria" enumerated in Question 45 – *i.e.*, organization, structure, capability of staff, and geographic location – China has provided no indication that foreign enterprises, foreign individuals and enterprises in China are incapable of fulfilling the annual inspection report requirements set forth in paragraphs 4 and 5 of Exhibit CN-22. Indeed, China has provided no reason to believe that these importers could not provide statistics on importation, hire qualified experts to conduct content review, supply GAPP with the required catalogue of imported reading materials, and identify to GAPP any prohibited content in the reading materials they are importing. Again, while content review is not integral to the importation process, one of the U.S. alternatives provides that all importers with qualified personnel could conduct content review of the products they import.

188. With reference to para. 116 of China's second written submission, please answer the following questions:

(a) Why could foreign entities not be held liable for the failure to prevent cultural goods with prohibited content being imported into China? Are

there ways in which China could enforce its content review rules even if the review is taking place outside of China? For example, could China seize any revenues resulting from the prohibited circulation of the relevant good or prevent an enterprise that breached content review requirements from importing the relevant goods into China in the future? Or could it require that foreign individuals or enterprises have a bank account in China which China could block in the event of a breach of relevant requirements?

58. Contrary to China's response to Question 188(a), each of the sanctions identified by the Panel would provide China with a basis to establish jurisdiction and to adequately deter breaches of its content review requirements. Moreover, China's argument regarding the insufficiency of targeting economic benefits lacks credibility. In fact, such economic benefits are at the core of China's own sanctions regime concerning violations of content review requirements. Each of the measures at issue addressing the importation of the products provides for monetary fines and the confiscation of illegal gains and illegal goods, when content requirements are contravened.[49]

(b) China has said that foreign entities may not fully understand the concept of public morals. However, China has also said that content review is about examining goods for specified prohibited content. In the light of this, since content review seems to be a rule-based process, why could foreign or Chinese private entities not adequately perform content review abroad?

59. China's response to Question 188(b) is fundamentally flawed. China states that "[foreign] entities could not be entrusted with performing content review abroad" because they "may not be fully aware of the precise scope of [Chinese] values" and may therefore incorrectly apply relevant content rules. China's argument, however, misses the point. The fact that a foreign entity is performing content review abroad is irrelevant. What is relevant is whether content review is being conducted for that foreign entity by a qualified expert. As long as the content reviewer is qualified, it does not matter where that reviewer is physically located or who employs that reviewer.

60. China also submits that neither foreign nor Chinese private entities could perform content review abroad because they could not be asked to bear that cost. The question of who should bear the cost of content review, however, is unrelated to the question of whether China has a rule-based content review process. The United States has identified three reasonably-available WTO consistent alternatives that comply with China's trading rights commitments to allow all foreign enterprises, all foreign individuals, and all enterprises in China to import the products,

[49] Management Regulation, Article 56 (Exhibit US-7); Audiovisual Regulation, Article 46 (Exhibit US-16); Audiovisual Import Rule, Article 33 (Exhibit US-17); and Film Regulation, Article 56 (Exhibit US-20).

while maintaining China's desired level of enforcement.[50] Moreover, the United States has demonstrated that there would be little, if any, additional costs imposed by these alternatives.[51] Finally, the United States stresses that China's content review system must not discriminate against imported products, and recalls that Chinese producers can conduct the content review of their own products.

189. With reference to para. 122 of China's second written submission, as an alternative, could the Chinese government certify trainers or training institutes and have importers demonstrate that relevant staff have successfully completed certified training courses?

61. In the context of the U.S. claims in this dispute, China's reluctance to explore ways to increase the number and quality of content reviewers is telling. Furthermore, while China has never explained how it imposes "direct control" over current content reviewers and why such control is integral to accurate content review, China simply assumes that the objectives of such control could not be achieved through Chinese government-certified trainers or training institutes. All new content reviewers could receive the same training given to current reviewers. As a deterrent to circumvention, content reviewers' certificates could be revoked where warranted.

62. The United States adds that China's response to Question 189 only implicates one of the three U.S. reasonably-available WTO consistent alternatives, *i.e.*, where content review is conducted by all importers regardless of national origin and Chinese Government ownership. Were content review to be conducted by the Chinese Government or by domestic Chinese entities, as is the case with respect to the other two U.S. alternatives, this would not affect the ability of all foreign enterprises, all foreign individuals, and all enterprises in China to import the products, since importation and content review would be separate and distinct.

190. With reference to para. 32 of China's second oral statement where China argues that "the right to import is the right to be licensed in order to organize the theatrical release of motion pictures." Please indicate whether the China Film Import and Export Corporation is licensed to organize the theatrical release of motion pictures. Likewise, please indicate whether China Film Group and Huaxia Film Distribution are importers of motion pictures.

63. The Panel's question is based on China's contention that with respect to films for theatrical release, "the right to import is the right to be licensed in order to organize the theatrical

[50] U.S. First Oral Statement, para. 35; U.S. Second Written Submission, para. 49; U.S. Second Oral Statement, paras. 25-37; and U.S. Answers to the Second Set of Panel Questions, paras. 74-81.

[51] U.S. Second Oral Statement, paras. 32-34.

release of motion pictures."[52] This is yet another attempt by China to contend that films for theatrical release are not goods subject to China's trading rights commitments. However, for the reasons the United States has set forth previously, this argument fails.[53] The fact that China Film Import and Export Corporation is licensed to organize the theatrical release of motion pictures in no way supports China's contention that that same entity is not also an importer of films for theatrical release. While an entity that imports a film for theatrical release may be licensed to organize the theatrical release of motion pictures, Article 31 of the Film Regulation provides that the "designated film importing entity" is also responsible for ensuring that the imported film is subject to the required customs procedures.[54] Thus, the right to import a film also includes the responsibility to subject the imported *good* to customs procedures.

191. At paras. 56 and 63 of China's second oral statement, China says that the content review is carried out at the importation stage by the importing entity. Please elaborate on what you mean by "at the importation stage". Is the relevant product cleared through customs before or after the content review has been successfully completed? If necessary, please distinguish between the various products at issue in this case (film, reading materials, etc.).

64. China's response to Question 191 further underscores the fact that content review is disassociated from the importation process and that content review can be conducted before, during or after that process. On the one hand, China explains that books, newspapers and periodicals are content reviewed in advance of importation. On the other hand, electronic publications, audiovisual products and films for theatrical release are imported and then reviewed. For example, films for theatrical release are imported, granted temporary customs clearance, reviewed, and then granted final customs clearance.[55] Thus, China itself confirms that importation and content review can and do occur independently.

192. With reference to paras. 30 and 55 of China's second oral statement, is China implying that its measures on reading materials or audiovisual products regulate the importation of goods, and that its measures on films and sound recordings intended for publication regulate the importation of content? If so, could China indicate how the text of the measures on the importation of reading materials and audiovisual products indicates this difference?

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[52] China's Second Oral Statement, para. 32.

[53] *See* U.S. First Oral Statement, paras. 9-18; U.S. Second Written Submission, paras. 18-20; U.S. Second Oral Statement, paras. 4-13.

[54] Film Regulation, Article 31 (Exhibit US-20).

[55] Film Regulation, Article 31 (Exhibit US-20).

65. China's argument that its measures related to reading materials and finished audiovisual products (including sound recordings) regulate the importation of goods while its measures on films and audiovisual products (including sound recordings) intended for publication regulate the importation of content is without merit and, in any event, in no way affects the analysis of the U.S. trading rights claims.

66. First, in response to the Panel's request to explain how the text of China's measures draw this distinction, China's discussion essentially boils down to the notion that because the measures relating to unfinished audiovisual products and films require the submission of certain copyright-related documents to the proper government officials, these measures are regulating content rather than a good.

67. China asserts that, based on these requirements, it is "clear[] . . .that these measures on audiovisual products distinguish between the importation of audiovisual goods and the importation of audiovisual content, which, similarly to motion pictures for theatrical release, are regulated on the basis of copyright licensing for the exploitation of this content."[56] However, nothing of the sort is "clear." These provisions requiring copyright documentation are simply added to the basic regime for importing goods – which applies to both finished and unfinished audiovisual products. For example, China has conceded that it applies customs duties to both finished and unfinished audiovisual products (including sound recordings).[57] China's own treatment of these products as goods is reinforced by Article 26 of the Audiovisual Import Rule, which provides that audiovisual product import units shall take certain approval documents for importing audiovisual products to Customs for the importation of "master tapes (master discs) or finished audiovisual products."[58] By referring to master tapes *i.e.*, unfinished audiovisual products, and finished audiovisual products, this provision makes clear that China treats both as goods. Similarly, Article 2 of the Audiovisual Import Rule explains that the measure covers "audiovisual products," which refers to "audio tapes, video tapes, records, and audio and video CDs *which have recorded contents* (see commercial names and *HS codes* in Attachment A)."[59] All of the products subject to the Audiovisual Import Rule have recorded contents, and all are treated as goods by China. Thus, the requirement to provide certain copyright-related documents in no way affects the analysis of whether a good is involved.

68. With respect to reading materials, China provides the text of Article 2 of the Management Regulation, which covers both reading materials and finished and unfinished "audiovisual products." China then states that because audiovisual products are also subject to audiovisual-

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[56] China's Answers to the Second Set of Panel Questions, Question 192.

[57] China's Answers to the First Set of Panel Questions, Question 132; *See also*, U.S. Answers to the First Set of Panel Questions, paras. 55-56.

[58] Exhibit US-17.

[59] Exhibit US-17 (emphasis added).

specific measures governing their importation, the Management Regulation only "regulates the importation of . . . reading materials as the importation of goods."[60] However, there is nothing in the text of the Management Regulation suggesting that the measure is distinguishing between the importation of goods with respect to some of the items listed and the importation of content with respect to other items. Moreover, both finished and unfinished audiovisual products are subject to the more specific measures governing the importation of audiovisual products and China admits that finished audiovisual products are goods. These facts mean that the distinction China draws here between the importation of content on the one hand and the importation of a good on the other does not withstand scrutiny.

69. In short, China makes certain assertions that its measures distinguish between the importation of goods as it relates to reading materials and finished audiovisual products and the importation of content as it relates to unfinished audiovisual products and films, but China fails to support any of these assertions. It is also noteworthy that China does not refer to a single measure challenged by the United States related to the importation of films for theatrical release.

70. As the United States has demonstrated, all of the Products that are the subject of the U.S. trading rights claim are goods[61] and China's restrictions on the entities that may import the Products are inconsistent with China's trading rights commitments.

193. Additionally, with respect to para. 30 of China's second oral statement, if China is implying that its measures on sound recordings intended for publication regulate the importation of content, do these measures also regulate finished sound recordings as content? Why?

71. The United States refers the Panel to its comment on China's response to Question 192.

194. With reference to footnote 16 of China's second oral statement, is Article 38 of the Administrative Licensing Law applicable generally to all approval or licensing processes, including those that are used to approve individuals or entities as importers of the products at issue in the US trading rights claims?

72. China's Administrative Licensing Law fails to address the U.S. trading rights claims. First, China states that this law only applies to the approval process, but not to the designation process. Only importers of books and electronic publications are "approved" by GAPP, but in addition to this approval, all of those importers are required to be wholly State-owned enterprises and to conform to the opaque State plan, pursuant to Article 42 of the Management Regulation.

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[60] China's Answers to the Second Set of Panel Questions, Question 192.

[61] *See* U.S. First Oral Statement, paras. 8-22; U.S. Second Written Submission, paras. 11-38; U.S. Second Oral Statement, paras. 4-14.

These requirements are inconsistent with China's trading rights commitments.[62] Importers of AVHE products, sound recordings and films for theatrical release are subject to the designation process, and importers of newspapers and periodicals are also designated by GAPP, in their case, from the pool of enterprises approved by that agency.[63]

73. Second, China has failed to explain why, or cite to any provisions demonstrating why, Article 38 of the Administrative Licensing Law is applicable to the approval and licensing of importers of the products at issue. Moreover, Article 38 of the Administrative Licensing Law has never been submitted as evidence in the form of an exhibit, which prevents review of its provisions, even though submission is required under the Panel's working procedures.[64] While the United States did include excerpts of the Administrative Licensing Law as Exhibit US-63, that exhibit does not include Article 38.

195. With reference to para. 33 of the US second oral statement, could China charge fees for the review of content in respect of all products relevant to this dispute? Alternatively, could foreign importers or privately owned importers in China charge the Government fees for the review of content if they were authorized to carry out content review in the same way as state-owned importers?

74. China's response fails to answer the first part of Question 195. Instead, China simply states that content review is "not only a matter of money". Of course, this is a change from China's previous position, when it argued that any other form of importation regime is cost-prohibitive from the standpoint of content review.[65] It appears that in the face of the U.S. responses, China is trying to move away from its previous position. China also cites "geographic coverage" and "efficiency" as another factor to be considered. China, however, fails to acknowledge that "efficiency" is also heavily resource-dependent. Moreover, it is not clear what China means by "geographic coverage" and in any case, China provides no explanation why having more, rather than fewer, content reviewers would not assist in addressing any such concerns.

75. Regarding the second part of Question 195, China explains that it should not be charged fees by non-governmental entities if those entities were to conduct content review. China arrives at this conclusion without explanation and then leaps into a discussion of why importers (presumably state-owned importers) should bear the "cost and losses" of content review. As the

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[62] U.S. First Written Submission, paras. 252-255; U.S. Answers to the First Set of Panel Questions, paras. 23-25; U.S. Second Written Submission, paras. 50-55; and U.S. Answers to the Second Set of Panel Questions, paras. 332-37 and 67-68.

[63] U.S. Second Written Submission, para. 54.

[64] Para. 14.

[65] China's Answers to the First Set of Panel Questions, Question 46(a); China's Second Written Submission, para. 104; and China's Answers to the Second Set of Panel Questions, Questions 185 and 188(b).

United States has explained, the three reasonably-available WTO consistent alternatives proposed by the United States would impose little, if any, additional costs.[66] In a non-discriminatory system, the costs of conducting the content review of imported products should be borne in the same way as the costs of conducting the content review of domestic products. In other words, importers should be treated no less favorably with respect to the cost of content review than domestic producers of like products.

196. With reference to para. 28 of the US second oral statement, is it correct that for AVHE products, sound recordings and films for theatrical release the Chinese government has exclusive jurisdiction over content review and is the only entity performing the review, and that for reading materials importers take part in the process but the Chinese government plays the central role?

76. The United States notes that China has supplied no evidence in support of its assertion that importers of AVHE products, sound recordings and films for theatrical release conduct a "preliminary review" of content in advance of the final decision provided by the Chinese Government. As explained in paragraph 28 of the U.S. second oral statement, the Chinese Government has exclusive jurisdiction over the content review of imported AVHE products, sound recordings and films for theatrical release.

77. Regarding the content review of imported reading materials, China fails to address Article 45 of the Management Regulation that requires GAPP to review all catalogues submitted by each importer listing all of the reading materials it is importing. Where GAPP identifies reading materials that are prohibited or "deferred" from importation, GAPP shall notify the importer and the Customs Administration. GAPP is not, therefore, limited to optional "additional" content review at the request of importers or at its own discretion, as China suggests.

<u>Questions to Both Parties</u>:

197. *With reference to para. 84(b) of the Working Party Report, please answer the following questions:

(a) Does the term "foreign enterprises" in para. 84(b) of the Working Party Report encompass foreign enterprises invested or registered in China? In your reply, please take into account the reference to "enterprises in China" in para. 84(a).

78. China's interpretation of the term "foreign enterprises" in paragraph 84(b) of the Working Party Report is overly narrow. As the United States explained in response to Question 197, both

[66] U.S. Second Oral Statement, paras. 32-34.

the plain meaning of this term and the context provided by paragraph 5.2 of the Accession Protocol support the inclusion of foreign enterprises invested or registered in China within the meaning of "foreign enterprises". China addresses neither of these issues.

79. In addition, the inclusion of the terms "all enterprises in China" and "foreign enterprises and individuals" in paragraph 84(a) indicates the intent of WTO Members that China's trading rights commitments be inclusive and comprehensive. China's interpretation of paragraph 84(b), however, would achieve the opposite result by limiting China's national treatment obligations only to foreign enterprises not invested or registered in China and possibly narrowing China's national treatment obligations under paragraph 5.2 of the Accession Protocol.

(b) Is the commitment that rights will be granted to foreign enterprises and individuals in a non-discretionary and non-discriminatory way substantively different from the obligation in para. 5.2 of the Protocol that foreign enterprises and individuals "shall be accorded" treatment "no less favourable" than that accorded to enterprises in China? If so, why and how?

80. China's response to Question 197(b) endeavors to unduly limit paragraph 84(b) by restricting its scope to non-discriminatory treatment between only foreign enterprises and individuals. There is no basis for such a limitation.[67] Nothing in the text limits China's obligation to provide non-discriminatory treatment between only foreign enterprises and individuals. The proper interpretation of paragraph 84(b) requires China to grant trading rights in a non-discriminatory manner as between foreign enterprises and individuals, and as between foreign enterprises and individuals on the one hand and enterprises in China on the other. Moreover, China committed to grant trading rights to all of these in a non-discretionary way.

(c) Para. 84(a) distinguishes between the three-year transition period (first sentence) and the period thereafter (second and following sentences). Does para. 84(b) set forth commitments that apply during or after the three-year transition period?

81. The United States has no comment on China's response to Question 197(c).

(d) The third sentence of para. 84(b) refers to "foreign enterprises and individuals with trading rights". Please explain why the phrase "with trading rights" was included. Does that phrase indicate that WTO-consistent requirements relating to importing and exporting may not restrict trading rights of foreign enterprises or individuals?

[67] U.S. Answers to the First Set of Panel Questions, para. 83; and U.S. Answers to the Second Set of Panel Questions, paras. 85-86.

82. Contrary to China's contention, the phrase "with trading rights" in the third sentence of paragraph 84(b) does not relieve the enterprises and individuals of WTO Members, which have yet to be granted trading rights, of their obligations with respect to WTO-consistent requirements, such as those concerning import licensing, TBT and SPS. As the United States explained in its response to Question 197(d), the phrase "with trading rights" recognizes that where China chooses to apply customs and fiscal requirements before granting trading rights, those actors that have not yet complied with those requirements would not yet have trading rights.

83. China also states that the phrase "with trading rights" "does not mean that WTO-consistent requirements relating to importing and exporting may not restrict trading rights". In its responses to Questions 159, 160(a), and 160(b), the United States has explained that China's trading rights commitments do not prejudice China's right to regulate trade. Therefore, China can require traders to comply with WTO-consistent measures that are directed at regulating goods being traded. The United States has recognized that the regulation of traded goods may have incidental effects on individual traders' trading rights. However, China's measures are fundamentally different from regulations on goods being traded. Unlike import licensing, TBT and SPS requirements which apply to goods, the measures at issue ban foreign importers and privately-held importers in China from importing the products at issue exclusively on the basis of national origin and Chinese Government ownership of the trader. In other words, China's trading rights restrictions bear no relationship to the products at issue or to the ability of these importers to import them.

198. With reference to para. 84(a) of the Working Party Report, please answer the following questions:

(a) Does the commitment set forth in para. 84(a) mean that within three years after accession China is to permit all foreign enterprises and individuals to export and import all goods, regardless of the treatment it accords to enterprises in China? In your reply, please take into account para. 5.2 of the Protocol.

84. China's response to Question 198(a) comports with the U.S. understanding of paragraph 84(a) of the Working Party Report and paragraph 5.2 of the Accession Protocol, with one exception. In its attempt to paraphrase paragraph 84(a), China states that it "would permit all enterprises in China and foreign enterprises and individuals to export and import all goods (*except as provided otherwise in the Accession Protocol*)."[68] The italicized text misstates China's commitment contained in paragraph 84(a), which provides "(except for the share of

[68] Emphasis added.

products listed in Annex 2A to the Draft Protocol reserved for importation and exportation by state trading enterprises)".

85. The United States also refers the Panel to the U.S. response to Question 198(a) for a further elaboration on the U.S. understanding of these two provisions.

(b) The first sentence says that China will eliminate its system of examination and approval of trading rights within three years after accession. How does this relate to para. 84(b) where it is stated that "any requirements for obtaining trading rights would be for customs and fiscal purposes only"? Are such requirements approval requirements? In replying to this question, please take into account para. 83(b).

86. China's response to Question 198(b) comports with the U.S. understanding that the customs and fiscal requirements referred to in paragraph 84(b) of the Working Party Report are not trading rights approval requirements.

199. With reference to para. 221 of the Appellate Body Report in EC - Bananas III (reproduced, e.g., at para. 21 of the US second written submission), please answer the following questions:

(a) Do the relevant Chinese measures governing the importation of film for theatrical release involve a service relating to a particular good or a good relating to a particular service? If the latter, how, if at all, would this affect what the Appellate Body said at para. 221?

87. In its response to Question 199(a), China demonstrates a fundamental misunderstanding of the Appellate Body's guidance in *EC – Bananas III*. First, China is wrong to invoke the Appellate Body when China says that measures, "which regulate services and only have an impact on goods as accessories to these services (and not as such), should only be examined under the GATS."[69] The Appellate Body neither said nor suggested that.

88. Instead, the Appellate Body's reasoning, as China itself notes, is that where a measure "could be scrutinized under both [the GATT 1994 and the GATS], the specific aspects of that measure examined under each agreement could be different. Under the GATT 1994, the focus is on how the measure affects the goods involved. Under the GATS, the focus is on how the measure affects the supply of the service or the service suppliers involved."[70] There is no basis in this guidance for China's novel and textually unsupported theory that a measure regulating

[69] China's Answers to the Second Set of Panel Questions, Question 199(a).

[70] *EC – Bananas III (AB)*, para. 221.

importation of a good is not subject to the goods disciplines where that good is used to provide a service. Moreover, China's argument that the relevant measures should not be subject to goods disciplines because the measures principally regulates services and only affects goods as an accessory to the service is explicitly contradicted by the Appellate Body's guidance.

89. The Appellate Body's reasoning makes clear that where a measure relates to trade in goods and services, the measure may be scrutinized under *both* goods and services disciplines; the elements of the measure governing trade in goods are subject to the goods disciplines and the elements of the measure governing the supply of services are subject to the services disciplines.[71]

90. China's consistent pattern as it relates to this line of argument has been to ignore the provisions of the relevant measures that regulate trade in goods and focus exclusively on the provisions that allegedly relate to services, or to ignore entire measures altogether that the United States challenges.[72]

91. In short, China has failed to rebut the U.S. *prima facie* case that the relevant measures, which limit who may import films for theatrical release, affect trade in goods in breach of China's trading rights commitments.

(b) Is there an inconsistency between the fourth sentence of the paragraph in question ("[i]n all such cases ... could be scrutinized") and its last sentence ("can only be determined on a case-by-case basis")? If not, why not?

92. The United States refers the Panel to the U.S. answer to Question199(b).

200. *For purposes of determining whether a measure is "necessary" within the meaning of Article XX of the GATT 1994, does the contribution to the realization of the objective pursued by a measure at issue need to be direct, or can it be indirect, i.e., via other requirements? Or to put it differently, does the measure at issue need to produce the desired effect by itself? To put this in context, there would appear to be two relevant requirements, an alleged restriction of the right to import and a requirement that importers conduct content review.

93. In its response to Question 200, China cites the Appellate Body report in *Korea – Beef* to contend that the measures at issue are "only required to 'contribute' to the realization of the objective pursued", in order to meet the "necessity test" of Article XX of the GATT 1994. China's incomplete reading of that report, however, leads it to the inaccurate conclusion that its measures are "necessary" within the meaning of Article XX(a).

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[71] U.S. Second Written Submission, paras. 21-25.

[72] U.S. First Oral Statement, para. 14; U.S. Second Written Submission, paras. 21-24; U.S. Second Oral Statement, para. 11.

94. To begin, China seems to suggest that as long as a measure makes some contribution to the realization of the objective pursued, it is automatically "necessary". While China cites paragraph 164 of the Appellate Body report in *Korea – Beef* for this proposition, China's selective interpretation misses the Appellate Body's reasoning that a series of factors are involved in determining whether a measure is necessary. Therefore, China's apparent reliance on the alleged contribution of its measures to the protection of public morals, to the exclusion of other considerations, is misplaced.

95. Furthermore, China neglects paragraph 161 of that report, in which the Appellate Body elaborates on the relationship between contribution and necessity. As the Appellate Body explains, a "necessary" measure is "located significantly closer to the pole of 'indispensable' than to the opposite pole of simply 'making a contribution to'."[73] Thus, China's contention that a measure only needs to contribute to the realization of the objective pursued in order to be necessary is fundamentally at odds with the very Appellate Body report China cites for its argument. Although the United States explained that a measure may be "necessary" even if it does not achieve the desired result all by itself, this is substantially different from China's view that any contribution by a measure, no matter how far from indispensable, is sufficient to make that measure "necessary". This tenuous connection is far too thin to support the weight of China's measures, which restrict trading rights in the name of content review when these two activities are disconnected in both concept and practice.

96. Finally, China fails to address the Appellate Body's discussion of reasonably-available WTO-consistent alternatives. In that paragraph, the Appellate Body states that a measure cannot be justified as "necessary" where a "WTO-consistent alternative measure which the Member concerned could "reasonably be expected to employ" is available.[74] The United States has proposed several reasonably-available WTO-consistent alternatives which demonstrate that China's trading rights prohibition is not "necessary".[75] While China tries to exclude one of those alternatives on the basis that the measures at issue are unrelated to content review, the United States has explained in its response to Question 165 that these alternatives are provided to rebut China's affirmative defense premised on an erroneous attempt to create an inextricable connection between importation and content review.[76]

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[73] *Korea – Beef (AB)*, para. 161.

[74] *Korea – Beef (AB)*, para. 165.

[75] U.S. First Oral Statement, para. 35; U.S. Second Written Submission, para. 49; and U.S. Second Oral Statement, paras. 25-37.

[76] U.S. Answers to the Second Set of Panel Questions, paras. 74-78.

DISTRIBUTION AND AUDIOVISUAL SERVICES

Questions to China

216. *Please comment on the US contention, in paras. 88 and 90 of its second written submission, that the Publication Market Rule and the Foreign-Invested Sub-Distribution Rule continue to maintain the prohibition on foreign-invested enterprises engaging in the master wholesale and wholesale of electronic publications.

97. China's response to Question 216 fails to rebut the U.S. arguments found in paragraphs 88 and 90 of it second written submission. With respect to the wholesaling of electronic publications, China's assertion that foreign-invested enterprises are allowed to engage in the wholesale of electronic publications is wholly inconsistent with its own responses to Questions 78 and 217. In response to Questions 78 and 217, China concedes that the Foreign-Invested Sub-Distribution Rule provides that "foreign-invested enterprises are prohibited from wholesaling imported *reading materials*"[77] (a term which includes electronic publications),[78] and that, consistent with Article 2 of that measure, only *books, newspapers and periodicals* published in China – and not electronic publications – are permitted to be wholesaled by foreign-invested enterprises.[79]

98. Moreover, China's assertion that the distribution, including wholesale, of electronic publications by foreign-invested enterprises is regulated exclusively by the Publication Market Rule (as of 2004) and then by the *Provisions on the Administration of Publishing Electronic Publications* (as of 2008) is also inaccurate and contrary to China's response to Question 91. In response to Question 91, China contends that after 2004 *both* the Publication Market Rule and the Foreign-Invested Sub-Distribution Rule govern the distribution of electronic publications by foreign-invested enterprises. As the United States demonstrated, however, the Publication Market Rule governs only *wholly Chinese-owned* distributors of electronic publications, while the Foreign-Invested Sub-Distribution Rule prohibits foreign-invested enterprises from distributing any reading materials, including electronic publications, other than *books, newspapers and periodicals* published in China.[80] Likewise, contrary to China's response to Question 216, the *Provisions on the Administration of Publishing Electronic Publications* (2008) govern only the publication, production and importation of electronic publications, and not their distribution.[81]

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[77] China's Answers to the Second Set of Panel Questions, Question 217 (emphasis added).

[78] U.S. First Written Submission, para. 3.

[79] China's Answers to the First Set of Panel Questions, Question 78.

[80] U.S. Second Written Submission, paras. 86-90.

[81] Article 2, (Exhibit CN-20).

99. Yet, even the underlying contention made in China's response to Question 91 is unsubstantiated. China merely asserts that the Electronic Publication Regulation ceased to govern the wholesaling of electronic publications by foreign-invested enterprises after 2004. China provides no argumentation as to why the Publication Market Rule or the Foreign-Invested Sub-Distribution Rule replace the Electronic Publication Regulation, and fails to refer to any provisions of either measure that might support China's conclusion. In fact, China's responses to both Question 91 and Question 216 are in direct conflict with China's first written submission, in which China states that the Electronic Publication Regulation was replaced by the *Provisions on the Administration of Publishing Electronic Publications* in 2008.

100. China's reliance on a 2005 GAPP response to its local counterpart in Shanghai is misplaced as well. This response is in direct contravention of Chinese law, whether that law is the Electronic Publication Regulation or the Foreign-Invested Sub-Distribution Rule. In contrast to a "practice" that China asserts to have existed since 2004, both of these legal instruments prohibit foreign-invested enterprises from wholesaling electronic publications.

101. China's response to Question 216 with respect to the master wholesaling of electronic publications also does not withstand scrutiny. As explained in the U.S. response to Question 211, China has failed to demonstrate that master wholesale was discontinued as a type of distribution after 1999. China's chief failing lies in the fact that it does not explain why the *Interim Provisions on the Administration of the Publications Market* render master wholesale non-existent and that it does not even submit this measure to the Panel. In addition, the Electronic Publication Regulation, which explicitly regulates the master wholesale of electronic publications, was in effect until 2008. Exhibits US-80, US-81 and US-104 further confirm that master wholesale continued to exist after 1999.

217. *With reference to paras. 66-72 of the US second written submission, does China agree with the US assertion that the identified measures prohibit foreign-invested enterprises from wholesaling imported reading materials?

102. China's response to Question 217 comports with the U.S. understanding that the Foreign-Invested Sub-Distribution Rule provides that "foreign-invested enterprises are prohibited from wholesaling imported reading materials."[82] The United States notes, however, that China failed to address the Panel's question with respect to all of the measure identified in paragraphs 66-72 of the U.S. second written submission. Moreover, as explained in the U.S. response to Question 216 above, China's responses to Questions 216 and 217 are completely contradictory.

218. *With reference to para. 82 of the US second written submission, is the United States correct in saying that master distributors (Zong Fa Xing entity) can resell reading

[82] China's Answers to the Second Set of Panel Questions, Question 217.

materials to "other wholesalers"? Please particularly comment on Exhibit US-56 and Exhibit US-57 in which, according to the United States, master distribution is defined as "first-level wholesale".

103. In response to Question 218, China asserts, without support, that master distributors "cannot resell to other wholesalers reading materials that are subject to" master distribution. This response is, however, belied by the Chinese legal instruments and other sources submitted by the United States that demonstrate that master distributors resell reading materials to other wholesalers.[83]

104. Regarding Exhibits US-56 and US-57, China again invokes the *Interim Provisions on the Administration of the Publications Market* to assert that the concept of "first-level wholesale" is inapplicable after 1999. China provides no explanation for why or how this is the case, nor does it submit this measure into the record for review or rebuttal.

219. *With reference to para. 82 of the US second written submission, is the United States correct in saying that master distributors can resell reading materials to "other wholesalers"? Please particularly comment on Exhibit US-56 and Exhibit US-57 in which, according to the United States, master distribution is defined as "first-level wholesale".

105. The United States has no comment on China's response to Question 219.

220. With reference to China's reply to Panel Question 102, please elaborate on what "retail shops under the Zong Fa Xing entity" means. Does it mean that the Zong Fa Xing entity owns or controls these shops?

106. China's response to Question 220 confirms that master distribution includes retailing, thus further confirming that master distribution is covered by China's market access and national treatment commitments under mode 3 of Sector 4C of its Services Schedule. For the reasons described in the U.S. response to Question 201, the U.S. claim under Article XVII of the GATS with respect to reading material includes China's discriminatory treatment of both wholesalers and retailers of these products.[84]

221. In answering Panel Question 93, China says that the Publication Zong Fa Xing Entity is an exclusive seller rather that an agent of the publisher. As a result, is it the case that the Publication Zong Fa Xing Entity purchases publications from the publisher and then resells them?

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[83] Exhibit US-56, Exhibit US-57, Exhibit US-58, Exhibit US-78, Exhibit US-99 and Electronic Publication Regulation, Article 2 (stating "[a]n electronic publication distribution entity must buy from an electronic publication publishing, import, *master wholesale*, or wholesale entity." (emphasis added)) (Exhibit US-15).

[84] U.S. Answers to the Second Set of Panel Questions, paras. 103-104.

107. China's response to Question 221 further confirms that master distribution includes "wholesaling" within the meaning of Annex 2 of China's Services Schedule, since master distributors purchase reading materials from publishers and then resell those products. Thus, China acknowledges that master distributors resell reading materials, including those in China's newly-introduced sub-category of reading materials "subject to master distribution". The United States notes that China referred to this new sub-category for the first time in these answers to the second set of Panel questions, and did not mention this alleged sub-category in its response to Panel Question 93.

108. In addition, China's response to Question 237 combined with its response to Question 221, fully concedes that master distribution of reading materials, including those allegedly subject to master distribution, includes "wholesale trade services" within the meaning of Sector 4B of China's Services Schedule. In its response to Question 237, China confirms that master distributors resell reading materials subject to master distribution to "industrial, commercial, institutional, or other professional business users". This category of purchaser is explicitly included in the definition of "wholesaling" in Annex 2 of China's Services Schedule.

222. In answering Panel Question 105, China says that the Zong Fa Xing entity supplies the end-consumer with reading materials without passing through any intermediary. What is the basis for this assertion?

109. China's contention that master distributors supply end-consumers with reading materials without passing through any intermediary is fully contradicted by several Chinese laws and other sources submitted by the United States that confirm that master distribution includes the reselling of reading materials to other wholesalers.[85]

110. Indeed, China's own definition of master distribution as "the exclusive sale of publications by a publication *Zong Fa Xing* entity" does not mean that master distributors cannot resell reading materials to intermediaries. Rather, China's definition provides that a master distributor has the exclusive right with respect to a certain title to sell that title. In other words, for book X, only one master distributor can sell copies of book X, but that master distributor can sell copies of book X to: other wholesalers; retailers; industrial, commercial, institutional, or other professional business users; or purchasers for personal or household consumption.

111. Finally, China incorrectly assumes that wholesaling requires reselling to an "intermediary". The definition of "wholesaling" found in Annex 2 of China's own Services Schedule contains no such requirement. Instead, under this definition, wholesaling can involve

[85] Exhibit US-56, Exhibit US-57, Exhibit US-58, Exhibit US-78, Exhibit US-99 and Electronic Publication Regulation, Article 2 (stating "[a]n electronic publication distribution entity must buy from an electronic publication publishing, import, *master wholesale*, or wholesale entity." (emphasis added)) (Exhibit US-15).

reselling to industrial, commercial, institutional, or other professional business users, which can be end-consumers.

223. With reference to paras. 85 to 90 of China's second oral statement, please explain why wholly-Chinese owned enterprises are not subject to the limitation on operating terms.

112. In its response to Question 223, China does not explain why wholly Chinese-owned enterprises are free of government-imposed operating term limitations. China merely explains that these enterprises may set their own operating terms, which begs the question why foreign-invested enterprises are denied the same liberty. As the United States has explained, this different treatment accords to foreign-invested enterprises treatment that is less favorable than that accorded to wholly Chinese-owned enterprises.[86]

113. Moreover, China's reference to a "governmental assurance of exemption from policy change", does not excuse the discriminatory nature of the operating term requirement. First, it is not clear what China understands as the meaning of this phrase. Second, China's operating term does not exempt foreign-invested enterprises from governmental policy changes. Chinese laws and policies governing foreign-invested distributors can change just as easily as Chinese laws and policies governing wholly Chinese-owned distributors. For instance, if relevant corporate taxes are increased, foreign-invested enterprises will have to pay higher taxes. Likewise, if accounting rules are updated or competition laws are amended, foreign-invested enterprises will have to make the necessary changes in order to comply. In the same vein, foreign-invested reading material distributors and foreign-invested AVHE distributors could be subject to policy changes regarding the operating terms of their enterprises.

114. Furthermore, the discriminatory operating term requirement is not cured by the possibility of extension. Despite China's assertions to the contrary in paragraphs 85-90 of China's second oral statement, extension is not "non-discretionary, automatic and simplified". Foreign-invested enterprises require not only additional government approval, which is subject to no objective criteria, but also agreement by all investors and directors and compliance with all laws, regulations and policies on foreign investment,[87] which presumably includes continued "friendliness".[88] While China alleges that the United States ignores the requirements pertaining

[86] U.S. First Written Submission, paras. 100, 128, 298 and 334; U.S. Answers to the First Set of Panel Questions, para. 99, and 133-134; U.S. Second Written Submission, paras. 93-97 and 135-139; and U.S. Answers to the Second Set of Panel Questions, paras. 136-139.

[87] U.S. Second Written Submission, paras. 95-97 and 135-139; and U.S. Answers to the Second Set of Panel Questions, paras. 137-139.

[88] Several Opinions, Article 6 (Exhibit US-6).

to investors and directors and foreign investment laws, regulations and policies, this statement is factually incorrect.[89]

115. Rather, it is China that fails to respond to the U.S. argument that the operating term requirements inject considerable uncertainty, as well as risk of termination, into the operation of foreign-invested enterprises, but not into the operations of wholly Chinese-owned enterprises. The United States also notes that China has cited to Article 38 of the Administrative Licencing Law,[90] which has not been submitted as evidence to the Panel, thereby preventing any review and rebuttal of that measure.[91]

224. *With reference to paras. 99 and 100 of the US second written submission, please confirm that under Chinese law, both foreign-invested and wholly-Chinese owned enterprises may contribute their registered capital in instalments over the same period of time.

116. In its response to Question 224, China confirms the inaccuracy of its single argument against the U.S. claim under Article XVII regarding China's discriminatory registered capital requirements imposed on foreign-invested distributors of reading materials.[92]

225. With reference to paras. 101 and 103 of the US second written submission, please address the US assertion that the pre-establishment legal compliance requirement contained in the identified measures imposes a more onerous hurdle to entry on foreign-invested wholesalers than Article 65 of the Regulations on Publishing.

117. China's response to Question 225 appears to accept that the pre-establishment legal compliance requirement imposed exclusively on foreign-invested wholesalers is more onerous than the requirements contained in Article 65 of the Management Regulation. In fact, the United States understands China's response to suggest that the pre-establishment legal compliance requirement applies to *all* legal violations in *all* of the countries in which the foreign-invested enterprise operates. The pre-establishment legal compliance requirement, therefore, is global in scope. Thus, as China admits, the pre-establishment legal compliance requirement is used at the government's discretion in deciding whether or not to approve foreign-invested distributors of reading materials and AVHE products.

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[89] U.S. Second Written Submission, paras. 94 and 137; and U.S. Answers to the Second Set of Panel Questions, paras. 137 and 139.

[90] China's Second Oral Statement, para. 87 footnote 16.

[91] *See* U.S. comment on China's response to Question 194 above.

[92] China's First Written Statement, paras. 295 and 318-319.

118. In stark contrast, Article 65 of the Management Regulation is far less broad, applying only to certain corporate officials employed by distributors whose licenses have been revoked as a result of violations of the Management Regulation.

119. Moreover, in its response to Question 225, China explains that a pre-establishment legal compliance requirement is not required for wholly Chinese-owned distributors, because the Chinese government is aware of the laws and regulations these distributors are subject to. This statement seems to ignore the fact that wholly Chinese-owned enterprises may also be subject to, and have violated, foreign as well as domestic laws and regulations. In addition, China fails to address the fact that when wholly Chinese-owned enterprises violate Chinese laws and regulations, there appear to be no equivalent legal mechanism to prevent wholly Chinese-owned enterprises from being approved to distribute reading materials and AVHE products.

226. With reference to para. 113 of the US second written submission, is it correct that only foreign-invested enterprises are subject to GAPP's decision-making criteria?

120. China's response merely reiterated its erroneous contention that the Several Opinions are internal guidance. Even if this was true, which it is not,[93] China failed to answer the Panel's question. In fact, China has never explained what such "internal guidance" is used for and why. Likewise, China fails to substantiate its assertion that the Several Opinions are not "enforced" by GAPP in its decision making. As the United States has explained[94] and China has not contested,[95] the Several Opinions are legally binding on the five agencies responsible for their issuance. These also are measures within the meaning of Article 3.3 of the DSU. The United States also takes this opportunity to correct China's statement that these decision-making criteria are found in Article 4 of the Several Opinions; they are actually set forth in Article 6 of that measure.

227. *With reference to para. 325 of the US first written submission and para. 119 of the US second written submission, please address the US assertion that both Exhibit US-6 and Exhibit US-9 confirm that the Chinese party to a Chinese-foreign contractual joint venture engaging in the sub-distribution of audiovisual products must hold the majority of the shares.

121. With respect to Question 227, China not only fails to answer the Panel's question, but also reasserts numerous flawed arguments.

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[93] U.S. First Oral Statement, para. 92; U.S. Second Oral Statement; paras. 219 and 220; Second Oral Statement, para. 84; and U.S. Answers to the Second Set of Panel Questions, paras. 1-9.

[94] U.S. First Oral Statement, para. 92; U.S. Second Written Submission, paras. 219-220; U.S. Second Oral Statement, para. 84; and U.S. Answers to the Second Set of Panel Questions, paras. 2-4 and 7-8.

[95] China's Answers to the Second Set of Panel Questions, Question 147.

122. To review the U.S. claims, the United States challenges the Audiovisual Sub-Distribution Rule, the Catalogue, the Foreign Investment Regulation and the Several Opinions under Article XVI:2(f) and Article XVII of the GATS. Article XVI:2(f) provides that "in sectors where market access commitments are undertaken, the measures which a Member shall not maintain or adopt . . . unless otherwise specified in its Schedule, are defined as . . . (f) limitations on the participation of foreign capital in terms of maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment."[96] In addition, Article XVII provides that "subject to any conditions and qualifications set out therein, each Member shall accord to services and service suppliers of any other Member . . . treatment no less favorable than that it accords to its own like services and service suppliers."[97]

123. In China's Services Schedule, China committed to permit foreign service suppliers to establish contractual joint ventures with Chinese partners to engage in the distribution of AVHE products. China did not include in its Schedule a limitation on the capital participation of the foreign party to the contractual joint venture. China also scheduled no limitations on national treatment as it relates to the distribution of AVHE products. Nevertheless, the relevant Chinese measures limit the participation of foreign capital in terms of the foreign party's percentage of shares and total investment in contractual joint ventures engaged in the distribution of AVHE products.

124. China has challenged the U.S. translation of two of the measures: the Catalogue and the Audiovisual Sub-Distribution Rule, and China has asserted, unsuccessfully, that its translations of these measures disprove the U.S. claim. China translates Article VI:3 of the "Catalogue of Restricted Foreign Investment Industries" as limiting the distribution of audiovisual products to contractual joint ventures where the Chinese partner "shall have controlling interest."[98] In addition, China translates Article 8(4) of the Audiovisual Sub-Distribution Rule as providing that "a majority of the rights and interests" in a Chinese-foreign joint venture engaged in the distribution of AVHE products shall be held by the Chinese partner. China then asserts that these provisions limit not the share of equity held by foreign partners in a contractual joint venture, but instead their share of profits and losses. However, the measures in question do not support this assertion, regardless of whether the U.S. or Chinese translation is used.

125. With respect to Article 8(4) of the Audiovisual Sub-Distribution Rule, China has not explained how the "rights and interests" held by a party to a Chinese-foreign contractual joint

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[96] *See* U.S. First Written Submission, paras. 319-25.

[97] *See* U.S. First Written Submission, paras. 124-26; 333.

[98] Exhibit CN-41. As provided in Exhibit US-5, the United States considers that Article VI:3 of the Catalogue of Restricted Foreign Investment Industries is appropriately translated as "Sub-distribution of audiovisual products (excluding motion pictures) [is] (limited to contractual joint ventures where the Chinese partner holds majority share)".

venture are synonymous with (and limited to) "profit" and "loss."[99] China has also not explained how a provision that limits the "rights and interests" that a foreign party may hold in a Chinese-foreign contractual joint venture rebuts the U.S. *prima facie* case that these measures are inconsistent with Article XVI or Article XVII of the GATS. Since this provision would appear to limit every element of the foreign party's participation in a contractual joint venture including percentage of shares, capital participation, and investment, China's translation of the measure does nothing to rebut the U.S. evidence that the provision is inconsistent with Article XVI of the GATS.[100] Moreover, because such a measure limits the "rights and interests" of the foreign party to 49% based solely on the national origin of that party, the measure also accords less favorable treatment to foreign service suppliers than to like wholly-owned Chinese service suppliers.

126. With respect to the Catalogue, China has failed to show how a different translation would disprove the evidence showing that China limits the share of equity held by foreigners. Even if the measure required the Chinese partner to possess the "controlling interest," that would not support China's contention that the *only* effect of the limitation is on the allocation of profits and losses. China's proffered translation not only fails to rebut the Article XVI inconsistency put forward by the United States, it also represents a concession that foreigners receive less favorable treatment than Chinese persons, which is inconsistent with China's commitments under Article XVII.

127. Furthermore, although Panel Question 227 asked China to address the U.S. challenge to the Several Opinions and the Foreign Investment Regulation, its response does not mention those measures, let alone analyze them.[101] The United States understands that China will be providing its translation of certain relevant provisions of these measures in its submission on October 24, 2008.

128. However, China does, in its answer to Question 227, repeat its argument based on the Law on Chinese-Foreign Contractual Joint Ventures.[102] China's reliance on that measure is, however, unavailing. Contrary to China's contention, Article 2 of the Law on Chinese-Foreign Contractual Joint Ventures makes no reference to the distribution of profits in a contractual joint

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[99] *See* U.S. Second Written Submission, paras. 122-23. In addition, the United States does not agree with China's translation of the relevant measure.

[100] As set forth previously, the United States considers that this provision is more appropriately translated as "A Chinese-foreign contractual joint venture for sub-distribution of audiovisual products shall meet the following conditions . . . (4) The Chinese cooperator shall hold no less than 51% equity in the contractual joint venture."

[101] Article 4 of the Several Opinions provides that "[u]nder the condition where the right of our country to examine the content of audiovisual products is not harmed, foreign investors are permitted to set up enterprises for the sub-distribution of audiovisual products, with the exception of motion pictures, in the form of Chinese-foreign contractual joint ventures where the Chinese partner holds a dominant position." (Exhibit US-6). Article 8 of the Foreign Investment Regulation provides that the term "have the Chinese party hold majority share" means "the total proportion of investment of the Chinese investor in the foreign-invested project is 51% and above." (Exhibit US-9).

[102] *See also* China's First Written Submission, para. 338.

venture. Nor does this measure provide that "the share of the profits, risks and losses is not required to be in proportion to each party's contribution of registered capital"[103] as China contends.

129. Even if it is correct that the Law on Chinese-Foreign Contractual Joint Ventures does not require that profits, risks and losses be in proportion to each party's contribution of capital, the United States is not asserting that it does. The United States is asserting that there are other measures that limit the percentage of shares that a foreign party to a Chinese-foreign contractual joint venture may hold. The existence of the Law on Chinese-Foreign Contractual Joint Ventures does not preclude the existence of other measures that place other limitations on the structure of Chinese-foreign contractual joint ventures, nor does it preclude the existence of other measures that place limitations on what the parties can agree to in their contract. Indeed, China is quite clear that based on its translation of Article 8(4) of the Audiovisual Sub-Distribution Rule, the parties to a contractual joint venture may not agree to give the foreign party more than 49 percent of the "rights and interests" in the entity.

130. China's reliance on footnote 1 of its Services Schedule is similarly unavailing. China notes that footnote 1 of China's Services Schedule provides that equity participation by all parties to the contractual joint venture is not required. However, the United States is not alleging a *requirement* of equity participation. Rather, the United States has demonstrated that a foreign partner faces percentage limitations when it *chooses* to invest equity in a contractual joint venture. Such a limitation is inconsistent with Article XVI:2(f) and Article XVII of the GATS regardless of whether equity participation is required.

131. In short, China's alternative translations of some of the measures at issue do not support its contention that participants in joint ventures are limited only in the percentage of profits and losses attributed to them. And, even if China's interpretation of these measures succeeded in avoiding a breach of Article XVI:2(f) of the GATS, the measures' inconsistency with national treatment remains clear.

228. With reference to China's reply to Panel Question 114 and Exhibit CN-100, China submits that Article (4) of the Measures on Audiovisual Products Distribution Joint Venture (Exhibit CN-54 and Exhibit US-18) should be translated as "The rights and interests in the contractual joint venture held by the Chinese co-operator is no less than 51 %." Please explain how, based on this translation, the above provision should be understood as referring to the allocation of profit and loss in contractual joint ventures. In your answer, please take into account footnote 1 of China's GATS Schedule. Also, if the allocation of profits and losses in contractual joint ventures is not based on equity participation of the parties, what is the basis for the allocation?

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[103] U.S. Answers to the Second Set of Panel Questions, Question 227.

132. In Question 228, the Panel asked China to explain how the terms "rights and interests" in Article 8(4) of the Audiovisual Sub-Distribution Rule, as translated by China, should be understood as referring to the allocation of profit and loss in contractual joint ventures. In response, China fails to provide any explanation. Instead, China merely repeats its assertion that "rights and interests" should be understood to refer to "profits and loss," but provides no support for such an assertion. For the reasons set forth in the U.S. comment on China's response to Question 227, China's arguments in this regard do not withstand scrutiny. Moreover, the example of a contractual joint venture (CJV) contract that China submits[104] fails to support China's argument.

133. While the example provided by China of a Chinese-foreign CJV engaging in the distribution of AVHE products[105] provides for the rate of distribution of profit for the parties to the CJV, it does not provide that the rate of profit received by the parties is synonymous with each party's interest or equity in the CJV. A close review of the contract makes clear that the foreign party's equity in the joint venture is, in fact, limited to less than 50%. First, Article 5.01 sets forth the amount of the registered capital of each party to the joint venture. As China correctly points out, the foreign party contributes 74% of the capital needed to set up the joint venture, well over half. However, Article 5.02(6) of the contract then states: "When Chinese laws and regulations permit the foreign party to legally hold a 50% *interest in the Company*, Party A will agree to Party C purchasing from Party A at any time a 1% interest in the Company."[106] Article 5.02(6) of the contract relates to the parties' ownership interest in the joint venture, not profit, which is addressed in Article 13.06 of the contract. This is reinforced by Article 5.05 of the contract, which relates to the parties' assignment or sale of their interest in the joint venture. Thus, Article 5.02(6) makes clear that the contracting parties were operating on the premise that Chinese laws and regulations do not currently permit the foreign party to hold a 50% interest. These provisions expose the inaccuracy of China's contention that the contract only relates to the parties' rate of distribution of profit, and not to equity or ownership interest. If the foreign party's equity were not so limited, there would be no need for Article 5.02(6) of the contract.

134. China's chart in response to Question 228 is, therefore, misleading because it suggests that the only element of the foreign party's participation that is limited is profit when, in fact, the contract clearly limits the ownership interest of the foreign party to less than 50%, consistent with the measures challenged by the United States.

135. Furthermore, China's statement that the allocation of "profits and losses in joint ventures is not required to be in proportion to equity participation and can usually be negotiated based on

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[104] Exhibit CN-107.

[105] Exhibit CN-107.

[106] Exhibit CN-107 (emphasis added).

other conditions for cooperation" fails to buttress China's defense that the measures challenged by the United States limit the foreign party's equity or shares in the CJV. The parties to a CJV may be free to negotiate certain conditions of the CJV; however, even under China's own understanding of the relevant measures, there are limitations on what the parties can agree. For example, the parties may not agree that the foreign party receives more than 49% of the rights and interests in the CJV. Indeed, the term "rights and interests" is so broad that a limitation on "rights and interests" would appear to be a limitation on every aspect of the foreign party's participation in the CJV including equity, shareholding, and total investment, not just profit. Moreover, the U.S. claim is not based on an assertion that equity must be in proportion to capital contribution. The U.S. claim is that where the foreign party to a CJV chooses to invest equity in a Chinese-foreign CJV, the foreign party faces percentage limitations. Such limitations on percentage of equity are inconsistent with Article XVI:2(f) of the GATS. Even if China's proffered translation were successful in avoiding a breach of Article XVI of the GATS, China's translation concedes that its measures accord less favorable treatment to the foreign party by limiting that party's rights and interests in a Chinese-foreign CJV. Accordingly, the national treatment inconsistency of these measures remains clear.

136. Finally, contrary to China's contentions, the fact that the Chinese party undertakes certain administrative responsibilities is irrelevant and does not somehow offset the limitation on the foreign party's "rights and interests" in the CJV.

229. With reference to para. 155 of China's second written submission, please explain when work started with a view to revising the Copyright Law that was adopted in 2001? In light of what developments was the decision to revise the law taken.

137. China's response to Question 229 confirms that, at the time of China's WTO accession, it was aware of the existence of the electronic distribution of sound recordings. The fact that China issued a draft amendment to the Copyright Law in December 2000, before its 2001 WTO accession is another fact demonstrating that at the time of its accession, China was aware of the emergence of the electronic distribution of sound recordings.

138. In response to Question 231, China contends that the relevant date for analyzing the circumstances surrounding the relevant treaty is November 15, 1999 because that is the date when the United States and China completed their bilateral negotiations, rather than 2001, when China actually acceded. However, China's Accession Protocol is a multilateral agreement. Accordingly, the date all of the parties concluded the agreement – 2001 – is the relevant date.[107]

[107] Even if November 1999 were the relevant date, it is difficult to accept China's suggestion that, although it had issued a draft law in December 2000 providing for certain copyright protections for the electronic distribution of sound recordings, thirteen months earlier it was completely unaware of the existence of that means of supplying the relevant service. *See* U.S. First Oral Statement, paras. 60-68; U.S. Second Written Submission, para. 154 n. 232.

139. At this time, China was aware of the emergence of the electronic distribution of sound recordings and China's discussion of the time line for developing copyright protections relevant to the electronic distribution of sound recordings only serves to highlight this reality.

230. With reference to para. 156 of China's second written submission, please indicate when you participated in the negotiations for the WIPO Copyright Treaty?

140. The United States has adduced numerous documents attesting to China's participation in multilateral fora, including the World Intellectual Property Organization (WIPO) and the WTO, discussing the electronic distribution of sound recordings.[108] As China itself concedes in response to Question 230, China participated in various meetings during the negotiation of the WIPO treaty, which was adopted in 1996.

231. With reference to para. 157 of China's second written submission, please comment on Exhibit US-85 and Exhibit US-100.

141. To place this question in context, the United States notes that Exhibit US-85 (the Cooperation Agreement of Beijing Artists Online Co. Ltd.) and Exhibit US-100 (the Houston Interweb Design, Inc., Form 10-KSB filed with the Securities and Exchange Commission), support the U.S. position that China was aware of the existence of the electronic distribution of sound recordings prior to 2001.

142. In the first oral statement, the United States rebutted China's contention that it was unaware of the electronic distribution of sound recordings by adducing considerable countervailing evidence, including evidence of the existence of a joint venture, Beijing Artists Online Co. Ltd., between a Houston-based company and the Chinese government.[109] The joint venture was established with the "objective to promote and develop Chinese music through the use of Houston InterWeb's advanced Internet technology both in China and overseas."[110] China responded by indicating that it was unaware of the existence of the joint venture.[111]

143. In light of Exhibits US-85 and US-100 documenting the existence of the joint venture, which the United States submitted with its second written submission, the focus of China's argument appears to have shifted. China now argues that the joint venture did not actually begin operations in China by mid-2001. China's argument misses the point, namely that at the time the government of China entered into the Cooperation Agreement in 2000, prior to China's WTO

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[108] U.S. First Oral Statement, paras. 61-67; U.S. Second Written Submission, para. 154 n. 232.

[109] U.S. First Oral Statement, para. 66.

[110] "MP3 Goes China – U.S. Company Inks Historical Internet Agreement with Chinese Government," *Business Wire* (February 29, 2000) (Exhibit US-61).

[111] China's Second Written Submission, para. 157.

accession, China was not only aware of the existence of the electronic distribution of sound recordings, but also actively sought to engage in the supply of that service.

144. Finally, the postponement of the launch of the joint venture's website in 2001, when many Internet companies were facing financial decline, does not support China's contention that the electronic distribution of sound recordings was not a commercial reality. This fact relates to the surrounding economic conditions at the time, not to the time line for the development of the electronic distribution of sound recordings.

232. With reference to paras. 317 to 319 of China's first written submission, could China explain why and how a flexible modality of payment is equivalent in terms of its impact on conditions of competition to, and could balance the effect of the higher registered capital requirement on foreign-invested entities?

145. In its response to Question 232, China repeats an argument from its first written submission that China itself has subsequently conceded. Thus, as China explained in its response to Question 224, both foreign-invested distributors and wholly Chinese-owned distributors can satisfy their registered capital requirements in installments. As China has confirmed that wholly Chinese-owned enterprises have equal access to such "flexible modalities of payment", China's response to Question 232 is inapposite. Moreover, the Unites States would note that Article XVII of the GATS does not permit the balancing of less favorable treatment with more favorable treatment in order to achieve some sort of "net" national treatment.

233. With reference to China's reply to Panel Question 107, is it China's position that the examination and approval procedures applicable to foreign-invested enterprises are inherent to the corporate forms as inscribed in the horizontal commitments of China's GATS Schedule? If so, please explain and indicate how this can be inferred from China's horizontal commitments.

146. China has not answered the Panel's question. The Panel asked whether the *examination and approval procedures* applicable to foreign-invested enterprises are inherent to the selected corporate forms, and if so, how this can be inferred from China's horizontal commitments. China does not, however, provide any analysis of the text of its horizontal commitment with respect to those procedures.

147. In fact, the correct answer to the Panel's question would be that any such "inherent"-ness cannot be inferred from those commitments, for the simple reason that the horizontal commitments, including footnote 1, say nothing at all regarding the examination and approval process applicable to the selected corporate forms. Instead, the horizontal commitments list the types of legal entity forms through which a foreign service supplier may supply a service, while footnote 1 provides that the terms of a contract for a contractual joint venture "govern" certain matters related to the operation of the joint venture. These sections of the schedule do not speak

to the measures governing the conditions of establishment of such corporate forms – let alone permit China to maintain measures that provide for more onerous examination and approval requirements for foreign-invested service suppliers. These facts suffice to dispose of China's contentions on this issue.

148. Unable to make an argument from the text of its schedule (as the Panel asked it to do), China argues instead that a limitation in its Services Schedule on the types of corporate forms through which a foreign service supplier may supply a service by itself permits China to maintain measures that deny national treatment on foreign service suppliers – even though those measures are not themselves mentioned or provided for in the Schedule.[112] China further states that "Article XVI:2(e) of the GATS does not impose any obligation on WTO Members intending to limit the available corporate form(s) to specify the conditions of establishment applicable for the selected types of corporate form(s)."

149. China's argument reflects a misunderstanding of the national treatment obligation in Article XVII of the GATS. Article XVII, in fact, does require that the conditions of establishment applicable for a type of corporate form be no less favorable than the conditions of establishment for a like domestic service supplier. Under Article XVII of the GATS, a limitation on national treatment in a scheduled sector is permissible only where that limitation is provided for in the Member's services schedule.

150. Many Members have inscribed limitations on the types of legal entity forms through which a foreign service supplier may supply a service (*i.e.*, limitations that – absent inscription in the Member's services schedule – would be inconsistent with GATS Article XVI:2(f)). The inscription of such a limitation, however, shelters that limitation, and nothing further. The United States expects that most WTO Members would be very surprised to discover that their acceptance in the Uruguay Round of a trading partner's requirement that a services supplier must take a particular legal form (for instance, a corporation, partnership, or joint venture) equated to an acceptance that that trading partner might also maintain other measures (*i.e.*, measures other than the simple form of legal entity requirement) that accord less favorable treatment to those service suppliers in all respects, including those not inscribed in the Member's schedule.

151. China did limit the types of forms of legal entity through which a foreign service supplier may supply a service. China did not, however, schedule a limitation on the capital participation or shareholding, operating term, or approval process applicable to such entities. Accordingly, measures that limit national treatment in those respects are inconsistent with China's obligations under Article XVII of the GATS.

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[112] In particular, China contends that the selected corporate forms "were embedded in a regulatory framework governing *inter alia* the conditions of establishment of such corporate forms in accordance with the relevant Chinese laws and regulations."

234. In para. 284 of its first written submission, China says that retailing services cover the reselling of goods or merchandise to end-consumers, contrary to wholesaling which covers the reselling to intermediaries in the distribution channel. However, it appears that the distinction between wholesaling and retailing services as defined in Annex 2 of China's GATS Schedule is not based on whether goods or merchandise are sold to end-consumers. Could China comment on this discrepancy?

152. China's distinction between wholesaling and retailing is at odds with the text of Annex 2 of China's own Services Schedule and fails to rebut the U.S. argument that master distribution includes wholesaling and retailing services. Annex 2 defines wholesaling as "the sale of goods/merchandise to retailers to industrial, commercial, institutional, or other professional business users, or to other wholesalers and related subordinated services." Annex 2 also defines retailing as "the sale of goods/merchandise for personal or household consumption either from a fixed location (*e.g.*, store, kiosk, etc.) or away from a fixed location and related subordinated services."

153. China argues in paragraph 284 of its first written submission that master distribution is not a type of wholesaling, because master distribution does not entail reselling to intermediaries. However, wholesaling within the meaning of Annex 2 is not defined in terms of reselling to intermediaries. In its response to Question 234, China itself concedes that wholesaling includes reselling to industrial, commercial, institutional, or other professional business users, which are not necessarily intermediaries. China has also confirmed that master distribution involves reselling to industrial, commercial, institutional, or other professional business users.[113] Moreover, the United States has also provided the Panel with numerous citations demonstrating that master distribution includes the reselling of reading materials to other wholesalers.[114] Thus, both wholesaling and master distribution, which includes wholesaling, involve reselling to both intermediaries and end-consumers. China, therefore, in fact has confirmed that master distribution is included in China's mode 3 commitments in Sector 4B of its Services Schedule.

154. In paragraph 284 of its first written submission, China also contends that master distribution is a type of retailing because master distribution involves the reselling of reading materials to end-consumers. While China is correct that master distribution may also include retailing, China's understanding of the term "retailing" goes beyond the text of Annex 2. Contrary to China's view, "retailing" within the meaning of Annex 2 is defined in terms of reselling to purchasers for personal or household consumption, rather than simply to end-consumers. Defining "retailing" in terms of reselling to end-consumers would conflict with the definition of "wholesaling", which can also include reselling to certain end-consumers.

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[113] China's Answers to the Second Set of Panel Questions, Question 237.

[114] Exhibit US-56, Exhibit US-57, Exhibit US-58, Exhibit US-78, Exhibit US-99 and Electronic Publication Regulation, Article 2 (stating "[a]n electronic publication distribution entity must buy from an electronic publication publishing, import, *master wholesale*, or wholesale entity." (emphasis added)) (Exhibit US-15).

155. The United States also takes this opportunity to recall that China has also conceded that master distribution is a type of retailing in its responses to Questions 102, 104, and 220. Thus, China has confirmed that master distribution is included in China's mode 3 commitments in Sector 4C of its Services Schedule. As explained in the U.S. comments on China's response to Question 220 above, the U.S. claim under Article XVII of the GATS with respect to reading material includes China's discriminatory treatment of both wholesalers and retailers of these products.[115]

235. With reference to para. 89 of the US second written submission, does China agree with the US assertion that the two GAAP approval decisions only apply to the wholesaling of domestic electronic publications?

156. China's response to Question 235 confirms that foreign-invested enterprises are not permitted to engage in the electronic publication wholesaling activities that China had asserted in its first written submission were available to them.[116]

236. Please comment on para. 106 of the US second written submission.

157. China states that the United States ignores Articles 7 and 8 of the Foreign-Invested Sub-Distribution Rule in paragraph 106 of the U.S. second written submission. Paragraph 106, however, addresses Article 12 of the Foreign-Invested Sub-Distribution Rule, which sets forth the MOFCOM approval process governing applications by foreign-invested enterprises to engage in the sub-distribution of books, newspapers and periodicals published in China. Article 12 contains no reference to using Articles 7 and 8 as the criteria for MOFCOM's decision making, much less any requirement that MOFCOM rely on, or limit itself to, the contents of those Articles in deciding whether or not to reject such applications.

237. Please comment on Exhibit US-99.

158. China's response acknowledges that master distribution includes wholesaling within the meaning of Annex 2 of its Services Schedule in its explanation that master distributors sell to

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[115] U.S. Answers to the Second Set of Panel Questions, paras. 103-104.

[116] Moreover, as the United States explained in paragraph 89 of its second written submission, the two GAAP approval decisions of 2006 are inconsistent with Chinese law, including the Electronic Publications Regulation (which China itself contends was not repealed until 2008) and the Foreign-Invested Sub-Distribution Rule. China has explained to the Panel that these last two measures prohibit foreign-invested enterprises from wholesaling electronic publications. (*See* China's Answers to the First Set of Panel Question, Questions 78 and 90; and China's Answers to the Second Set of Panel Questions, Question 217). The Electronic Publications Regulation explicitly states that foreign-invested enterprises are not permitted to wholesale and master wholesale electronic publications, and the Foreign-Invested Distribution Rule provides that only books, newspapers and periodicals published in China may be wholesaled by foreign-invested distributors. (*See* Electronic Publications Regulation, Article 62 (Exhibit US-15); and Foreign-Invested Sub-Distribution Rule, Article 2 (Exhibit US-28).

industrial, commercial, institutional or other professional business users. Moreover, several Chinese legal and other sources submitted by the United States verify that master distribution includes wholesaling, since it involves reselling to other wholesalers.[117]

238. Please comment on para. 52 of the US second oral statement.

159. In paragraph 52 of the U.S. second oral statement, the United States explained that the measures relevant to the U.S. claim under Article XVII of the GATS as it relates to the electronic distribution of sound recordings, relate to the distribution of sound recordings over the Internet and "other electromagnetic means." The United States also provided an interpretation of the Network Music Opinions posted on the Chinese Ministry of Culture's website confirming that the term "network" refers not only to the Internet, but also to "information networks, including telecommunication network, mobile Internet, cable television network, satellite communications, microwave communication, optical fiber communication, as well as other various interconnection between intelligent networks whose interaction is achieved based on the IP protocol."[118]

160. While China seeks to dismiss the relevance of this interpretation, the Chinese government has posted this interpretation on its website, which suggests that the Chinese government perceives the interpretation as credible.

161. More fundamentally, the Network Music Opinions itself refers to "[m]usic products transmitted through such wired or wireless media as the internet and mobile communications . . ."[119] Moreover, while China identifies a few examples of the use of the word "Internet" in the measure, China's attempt to limit the scope of the measure to transmission over the Internet ultimately fails.

162. Appendix 2 of the Network Music Opinions, as translated by China sets forth the content review procedures for imported audiovisual products "[f]or dissemination via *information network*."[120] As made clear by both Article I(1) of the Network Music Opinions itself and the interpretation submitted by the United States, the meaning of "information network" is broader than merely the Internet and also covers "other wired and wireless media as. . . mobile

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[117] Exhibit US-56, Exhibit US-57, Exhibit US-58, Exhibit US-78, Exhibit US-99 and Electronic Publication Regulation, Article 2 (stating "[a]n electronic publication distribution entity must buy from an electronic publication publishing, import, *master wholesale*, or wholesale entity." (emphasis added)) (Exhibit US-15).

[118] Interpretation of the "Several Opinions of the Ministry of Culture on the Development and Management of Network Music" (excerpt), available at: http://www.ccnt.gov.cn/xwzx/whbzhxw/t20061211_32441.htm (Exhibit US-101).

[119] Network Music Opinions, Article I(1) (Exhibit US-34).

[120] Exhibit CN-68 (emphasis added).

communications."[121] Accordingly, the few references to the "Internet" in various provisions of this measure that China points out fail to substantiate China's assertion that the measure only covers transmission over the Internet. The measure, in fact, is more broadly applicable to dissemination over the "network " *i.e.*, "such wired or wireless media as the internet and mobile communications," as the title of the measure suggests.

Questions to Both Parties

239. *Please address whether the terms "distribution services" in section 2.D of China's schedule of specific commitments could be interpreted as meaning the same as - or as encompassing - "distribution services" as used under CPC 96113? Please explain why or why not, in reference to the phrases "sound recording distribution services" and "videos, including entertainment software and (CPC 83202), distribution services" as they appear in China's Schedule of specific commitments.

163. For the U.S. views concerning the services covered by CPC 96113, the United States refers the Panel to the U.S. answer to Question 239.

164. The United States also notes that China provides no support for its contention, in response to Question 239, that its commitments under Sector 2D only cover distribution of goods in physical form.

240. *Please explain how sound recordings as physical products, as well as videos and entertainment software as physical products can be covered by sector 2.D. of China's schedule in view of the fact that sector 4 (including Annex 2) does not expressly specify that the distribution of any particular good is excluded from the scope of the commitments. In your explanation, please make reference to the AB's discussion in Gambling (found at para. 180) on the mutual exclusiveness of sectoral commitments.

165. First, both the United States and China agree that Sector 2D is the relevant sector in China's schedule for determining the meaning of its commitments with respect to hard-copy AVHE products and sound recordings.[122]

166. With respect to China's reliance on Korea's schedule, the United States considers that China's argument is misplaced. As a threshold matter, both parties agree that an analysis of the scope of China's commitment for sound recording distribution services is the text of China's

[121] Exhibit US-34. *See also* Interpretation of the "Several Opinions of the Ministry of Culture on the Development and Management of Network Music" (excerpt), available at: http://www.ccnt.gov.cn/xwzx/whbzhxw/t20061211_32441.htm (Exhibit US-101).

[122] China's Answers to the Second Set of Panel Questions, Question 240; U.S. Answers to the Second Set of Panel Questions, paras. 182-84.

schedule,[123] not any other Member's schedule. The text of Korea's schedule is not the same as China's schedule, contrary to China's contention.

167. China's schedule contains a commitment for "sound recording distribution services." In contrast, Korea's schedule contains a commitment for "record production and distribution services (Sound Recording)". The United States has provided an analysis under Article 31 of the Vienna Convention of the meaning of the relevant terms in China's schedule.[124]

168. Whether Korea's commitment for record production and distribution services covers the electronic distribution of sound recordings would require a separate analysis in accordance with the customary rules of treaty interpretation under the Vienna Convention, including an analysis of the meaning of the terms in Korea's Schedule in the relevant context (and that analysis is in any case not within the terms of reference of this Panel). Even if it were true that Korea's commitment did not cover the electronic distribution of sound recordings, that would not establish that China's commitment on sound recording distribution services should be interpreted as having the same meaning.

241. With reference to CPCprov subclass 96113 and its explanatory note, assuming arguendo that these might be relevant to the interpretation of commitments, please answer the following questions:

(a) What do the services described consist of? Are these different than in CPC ver. 1.1 subclass 96142?

169. The United States refers the Panel to its answer to Question 241(a) for a discussion of the meaning of Provisional CPC subclass 96113 and CPC ver. 1.1 subclass 9614.[125] The United States considers that Provisional CPC Subclass 96113 does not include sale or rental to the general public. Instead, Provisional CPC Subclass 96113 includes sale or rental of motion picture or video tapes *to other industries* for public entertainment or television broadcasting or for sale or rental to others. In other words, the other industries that purchase or rent the motion pictures or video tapes may sell or rent those items to others. However, the service classified in CPC Provisional 96113 itself does not include sale or rental to the general public.

(b) In referring to the sale or rental of "motion pictures or video tapes", is the explanatory note referring to the sale or rental of goods or of services?

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[123] China's Answers to the Second Set of Panel Questions, Question 239; U.S. Answers to the Second Set of Panel Questions, para. 124.

[124] U.S. First Oral Statement, paras. 52-53.

[125] The United States, like China, understands the Panel's question to be referring to CPC Subclass 96141, rather than 96142.

170. The United States considers that the Explanatory Note for Provisional CPC 96113 refers to the sale or rental of goods.[126] To the extent that China contends that Provisional CPC 96113 covers the sale or rental of goods and services because China considers motion pictures to be items other than goods, the United States has set forth in detail the reasons that China's arguments in this regard fail.[127]

(c) Do the services covered in CPCprov subclass 96113 involve reselling?

171. China asserts that the reselling of video tapes falls within Provisional CPC subclass 96113, but makes no mention of motion pictures, and provides no analysis to support this distinction between motion pictures and video tapes. The Explanatory Note describes the services classified in Provisional CPC subclass 96113 as covering "the sale or rental of movies or tapes to other industries for public entertainment, television broadcasting, or sale or rental to others." As the United States set forth, in response to Question 241(c), the services in Provisional CPC subclass 96113 cover reselling of motion pictures and video tapes.[128] The phrase, "or sale or rental to others," shows that the Provisional CPC subclass 96113 contemplates that after the sale to "other industries," those "other industries" may, in turn, sell the relevant items to "others." There is no reason to conclude that this reselling *i.e.*, the "sale or rental to others", does not refer to both motion pictures and video tapes.

(d) Is it customary, or at least possible, to provide the type of distribution services described in CPCprov subclass 96113 in respect of sound recordings as well?

172. In addition, China provides no analysis of subclass 96113 to support its assertion that the types of services contained therein only relate to physical items. For the reasons set forth in the U.S. response to Question 241(d), it is possible to provide the types of distribution services described in CPC provisional subclass 96113 in respect of sound recordings.[129]

242. *What is your interpretation of the term "CPC 83202" in China's commitment under section 2.D of its schedule?

(a) Please explain how "video (...) distribution services" could be meant to include "rental and leasing services of video tapes"?

173. The United States has no comment on China's response to Question 242(a).

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[126] U.S. Answers to the Second Set of Panel Questions, para. 189.

[127] U.S. First Oral Statement, paras. 8-18; U.S. Second Written Submission, paras. 12-29.

[128] U.S. Answers to the Second Set of Panel Questions, para. 190.

[129] U.S. Answers to the Second Set of Panel Questions, para. 191.

(b) Is it your view that the inclusion of the terms "CPC 83202" in China's schedule means that, subject to limitations scheduled, a foreign supplier could, for example, establish in China to provide the service of renting videotapes to the general public? If not, why not? Does it cover anything else?

174. The United States and China agree that the inclusion of "CPC 83202" in Sector 2.D of China's Services Schedule means that, subject to limitations scheduled, a foreign supplier could establish in China to provide the service of renting videotapes to the general public.

175. However, as set forth in the U.S. response to Question 242(b), the word "predominantly" in the Explanatory Note suggests that the subclass 83202 may also cover additional activities. Specifically, the Explanatory Note for this CPC subclass provides that this subclass includes "[r]enting or hiring services concerning pre-recorded video cassettes for use in home entertainment equipment *predominantly* for home entertainment."[130]

ARTICLE III:4 OF GATT 1994

Questions to China

264. Please respond to para. 176 of the US second written submission, by explaining how GAPP determines whether a publication falls within the limited distribution category, provide additional examples (other than Epoch Times) of publications in this category, and explain if titles can ever be moved from the limited distribution category to the non-limited distribution category.

176. The United States notes that China continues to assert without any support that the "limited distribution category" for reading materials addressed in the Imported Publications Subscription Rule consists of reading materials with prohibited content. The United States also submits that China has not justified the discriminatory treatment of imported reading materials confined to this opaque distribution category. Further, the United States notes that even if China were correct, and the less favorable treatment accorded to these imported reading materials was not designed to protect domestic reading materials against competition from foreign products, China has not met its burden with respect to any defense in response to the U.S. claim regarding the measures at issue.

265. With reference to para. 132 of China's second oral statement, please explain whether "titles" falling in the restricted category refers to (i) every issue of a particular

[130] Emphasis added.

newspaper or periodical; (ii) individual issues of a given newspaper or periodical that contain prohibited content; or (iii) both.

177. China's response to Question 265 underscores the extent of the discriminatory treatment accorded to imported reading materials confined to the "limited distribution category", as set forth in the Imported Publication Subscription Rule. Given China's estimate that there are approximately 1,000 imported titles in the "limited distribution category",[131] the total number of affected reading materials is thus quite significant.

266. *With respect to paras. 177 and 178 of the US first written submission and China's answer to Panel Question 130(a), please explain why it concludes that the term "entity" used in Article 6 of the Imported Publications Subscription Rule is different from the use of that term in other provisions of the same measure. Please explain whether China's statement, in para. 134 of its second written submission, that "the approval of entities to be able to susbscribe to publications in the restricted category is determined by GAPP on a case-by-case basis and in fact, may only be granted to certain government agencies and institutions" has a legal basis other than Article 6 of the Imported Publications Subscription Rule.

178. In response to Question 130(a), in which the Panel asked China for the basis of its assertion that only government agencies and government institutions are allowed to subscribe to reading materials in the "limited distribution category", China replied that the term "entity" used in Article 6 of the Imported Publication Subscription Rule provides that basis. The United States, however, has demonstrated that the term "entity" provides no such textual basis for China's assertion and that China has provided no additional argumentation or factual support to sustain that assertion.[132]

179. China responds to Question 266 with a new theory, *i.e.*, that Article 6 allows GAPP to select which domestic entities can subscribe to reading materials in the "limited distribution category". In other words, China appears to be stepping back from its view that the term "entity" is inherently limited to government agencies and government institutions. Instead, China suggests that GAPP may, in practice, only select government agencies and government institutions to subscribe to reading materials in the "limited distribution category". Yet, China's new theory suffers from the same absence of textual basis or other supporting argumentation or evidence as its original response to Question 130(a) did.

267. *In response to Panel Question 130(e), China explained that individual subscribers for newspapers and periodicals have to subscribe through the entities in which they work.

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[131] China's First Written Submission, para. 545.

[132] U.S. Second Written Submission, paras. 177 and 178.

Please explain with more detail how the subscription process for individuals works or "serves". For example, who pays for the subscription, the employer or "entity" or the individual? What if an individual has no employer, such as a student or a retired person? Does the law envisage that the employer has a say in whether an employee can subscribe to a particular newspaper or periodical? How do foreign residents in China subscribe to publications?

180. In response to Question 267, China states that the entity which individual subscribers "serve" "does not have any say in whether a domestic individual can subscribe to a particular imported newspaper or periodical in the "non-limited distribution category". China fails to provide any support, however, for this contention. Moreover, China offers no explanation why imported newspapers or periodicals in the "non-limited distribution category" can only be obtained by domestic individuals through a subscription acquired through the entity they "serve", when the same onerous condition is not imposed on domestic newspapers or periodicals.

268. Please respond to the US contention, in para. 199 of its second written submission and its response to Panel Question 138, that China's reasoning - that because movie-goers purchase the right to attend a screening rather than purchasing the film itself, there is no distribution under Article III:4 - is flawed.

181. In response to Question 268, China fails to actually answer the Panel's question. However, China repeats several erroneous assertions that have been addressed.

182. First, contrary to China's contention, the United States has not asserted a new claim under Article III:4. China maintains numerous measures that accord less favorable treatment to imported films for theatrical release than the domestic like products and these measures affect the internal sale, offering for sale, purchase, transportation, distribution or use of the imported product as required to make a claim under Article III:4.[133] These measures have been the subject of the U.S. claim throughout this dispute. Whether these measures affect the distribution or use of the imported product are arguments in support of the claim, not separate claims. Thus, the U.S. claim itself has not changed.

183. The United States has also explained in detail that the imported product is distributed in China, such that the measures affect the distribution of the imported product within the meaning of Article III:4 of the GATT 1994.[134] Thus, China's reasoning that "the distribution of motion

[133] U.S. First Written Submission, paras. 374-76, 382, 397-409; U.S. Second Written Submission, paras. 198-99; U.S. Answers to the First Set of Panel Questions, paras. 262-70; 271-75; U.S. Second Oral Statement, paras. 64-66; U.S. Answers to the Second Set of Panel Questions, paras. 253-57.

[134] U.S. First Written Submission, para. 382; U.S. Answers to the First Set of Panel Questions, paras. 262-75; U.S. Second Written Submission, paras. 196-98; U.S. Second Oral Statement, paras. 64-66; U.S. Answers to the (continued...)

pictures for theatrical release consists of the provision of services for the organization of public shows . . . and not distributing a good" is faulty, since it ignores the fact that the imported good is distributed.

269. With respect to China's answer to Panel Question 132, please provide an example of how it values for customs purposes an import of (1) the hard-copy sound recording intended for electronic distribution; (2) the hard-copy audiovisual product (including sound recordings) intended for publication; and (3) the exposed and developed cinematographic film) (China could provide an actual example of the customs valuation of a real sound recording intended for electronic distribution, audiovisual product for intended publication, and exposed and developed cinematographic film, or a description of the types of documentation its Customs authority uses to determine the customs value of the imported items)?

184. In response to Question 269, China made clear that it applies customs duties to unfinished sound recordings and hard-copy cinematographic film – both of which are tangible items containing content. Specifically, China confirms that "[a]ccording to the relevant Chinese measures concerning customs valuation, customs evaluation price includes royalties paid for copyright in connection with software, words, music, graphics, images, or other similar contents which are *contained in imported goods* in the form of tape, disk, compact disk, or other similar media."[135]

185. Accordingly, even under Chinese law, the fact that these items contain content, are subject to copyright licensing laws, and are commercially exploited through a series of services does not exempt them from customs duties, which confirms the U.S. position that these items must be treated as "goods."

270. *With reference to para. 201 of China's second written submission and Article III:4 of the GATT 1994, if it is accepted arguendo that the supply of goods to the Internet Culture Provider amounts to "distribution" within the meaning of Article III:4, could a measure regulating a product which is the result of further processing of the imported product (e.g. digitalized products, as China calls them) be said to "affect" the internal distribution of the imported product (e.g., the hard-copy of sound recordings for digital distribution)?

186. In its response to Question 270, China misunderstands the U.S. Article III:4 claim as it relates to imported hard-copy sound recordings intended for electronic distribution. First, the relevant measures affect the distribution of the imported hard-copy sound recording intended for

[134] (...continued)
Second Set of Panel Questions; paras. 253-57.

[135] China's Answers to the Second Set of Panel Questions, Question 269.

electronic distribution for the reasons set forth previously by the United States.[136] China's contention that the measures only affect the digitalized content overlooks the fact that the imported hard-copy sound recording is distributed within the meaning of Article III:4. Second, China's arguments proffer an overly rigid interpretation of Article III:4 that would allow Members to circumvent the national treatment disciplines afforded by that provision of the GATT 1994.[137]

187. Finally, the U.S. response to Question 256 reveals the flaws in China's attempt to rebut the U.S. claim with the hypothetical measure raised in China's second oral statement. This hypothetical fails to demonstrate that the Chinese measures at issue in this dispute do not affect the distribution of the imported product. Specifically, China set forth an example of a measure that prohibited broadcastings of sound recordings imported in hard-copy form but permitted the broadcasting of domestic sound recordings. Contrary to China's views, such a measure *would* appear to affect the internal sale, offering for sale, purchase, transportation, distribution or use of the imported product within the meaning of Article III:4 because the measure appears to limit the commercial opportunities available to the imported product *vis-a-vis* the domestic product.[138]

188. However, China states that under the U.S. interpretation of the "affecting" requirement in Article III:4, "a hypothetical measure regulating the broadcasting of foreign music through radio stations . . . would then have to comply with Article III:4 of the GATT for the simple reason that it might 'affect' the physical carriers purchased by the radio station."[139] In this answer, China regrettably continues on its course of inventing and discussing hypotheticals rather than the measures at issue. Nevertheless, to the extent that such a Chinese measure accorded less favorable treatment to imported hard-copy sound recordings (or other "physical carriers" to use China's term in this answer) than to the domestic like product by providing those imported products with less advantageous commercial opportunities affecting their internal sale, offering for sale, purchase, transportation, distribution or use, such a measure would likely be inconsistent with China's obligation under Article III:4 of the GATT 1994.

271. In response to Panel Question 13(a) the United States says that it is typically internegatives or interpositives, i.e., master copies, that are sent by licensors to distributors. In light of this statement, would it be incorrect to say that a licensor is "distributing" internegatives or interpositives to distributors, whereas a distributor is

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[136] U.S. Second Oral Statement, paras. 54-63; U.S. Answers to the Second Set of Panel Questions, paras. 212-22, 278-80.

[137] *See* U.S. Second Oral Statement, paras. 57-62; *See also Mexico – Taxes on Soft Drinks (Panel)*, para. 8.108 (the term "affecting" in Article III:4 "covers not only laws or regulations which directly govern the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between domestic and imported products").

[138] U.S. Answers to the Second Set of Panel Questions, para. 262.

[139] China's Answers to the Second Set of Panel Questions, para. 270.

"distributing" prints made from internegatives or interpositives to local cinemas? If so, why?

189. As set forth in detail by the United States, the imported product – typically the internegative or interpositive – is distributed in China.[140] Moreover, China's regime limiting the entities that may distribute films for theatrical release accords less favorable treatment to imported products regardless of whether the imported product undergoes further processing before it may be distributed to the ultimate consumer. Film prints made in China from an imported internegative face less advantageous distribution opportunities than film prints made in China from a domestic internegative. Under such a scenario, the conditions of competition are skewed against the imported internegative because a film print made from a like domestic internegative does not encounter the distribution obstacles that a film print made from the imported internegative does.[141]

190. China begins its answer to Question 271 by asserting that "the movement of cinematographic film is not relevant for the purpose of analyzing this claim under Article III:4 of the GATT. What is relevant is the distribution of the content, irrespective of the physical carriers that may be used and the various forms that they may take in the successive steps of the distribution of the motion picture." China provides no support for this assertion nor does China even make it clear how this relates to the U.S. claim. While China has gone to great lengths to try to separate the content from the good as it relates to films for theatrical release, the United States has done nothing of the sort. The hard-copy product that is imported – cinematographic film – is distributed within the meaning of Article III:4 of the GATT 1994 for the reasons the United States has set forth in detail.[142] The measures limiting the distribution opportunities for such imported products, as compared to the domestic like products, are inconsistent with the national treatment obligation in Article III:4 of the GATT 1994.

191. Moreover, a finding that the measures limiting which entities may distribute the imported product does not affect the imported product because the product undergoes further processing

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[140] U.S. First Written Submission, para. 382; U.S. Answers to the First Set of Panel Questions, paras. 262-75; U.S. Second Written Submission, paras. 196-98; U.S. Second Oral Statement, paras. 64-66; U.S. Answers to the Second Set of Panel Questions; paras. 253-57.

[141] *See Mexico – Soft Drinks (Panel)*, para. 8.108 (The term "affecting" "covers not only laws and regulations which directly govern the conditions of sale or purchase but also any laws or regulations which might adversely modify the conditions of competition between domestic and imported products.").

[142] U.S. First Written Submission, para. 382; U.S. Answers to the First Set of Panel Questions, paras. 262-75; U.S. Second Written Submission, paras. 196-98; U.S. Second Oral Statement, paras. 64-66; U.S. Answers to the Second Set of Panel Questions; paras. 253-57.

downstream would create a loophole in the national treatment disciplines afforded by Article III:4.[143]

272. Please clarify the point that is being made at para. 136 of China's oral statement. In particular, please explain the reference to directly applicable rules and regulations of various departments that "may even run contrary to the 'Imported Cultural Products Measures'". Is China saying that the Imported Cultural Products Measure permits various departments to maintain rules and regulations contrary to it or that some departments may not yet have amended their rules and regulation so as to conform to the Imported Cultural Products Measures?

192. China's arguments contained in paragraph 136 of its second oral statement and in its response to Question 272 are unsuccessful in rebutting the U.S. claim regarding the discriminatory treatment accorded to imported newspapers and periodicals in the "non-limited distribution category". As the United States has shown, imported newspapers and periodicals in the "non-limited distribution category" can only be obtained through subscription by subscribers that have been examined and approved by the Chinese government.[144] As part of its argument, the United States has cited Article 14 of the Imported Cultural Products Measure, which states in relevant part, "[d]omestic units and individuals inside China who wish to subscribe to outside newspapers and periodicals from newspaper and periodical import units must go through examination and approval procedures."[145]

193. In paragraph 136 of its second written submission and in its response to Question 272, China asserts that the Imported Cultural Products Measure is not directly applicable to importation and subscription activities and that it is not enforced by its issuing agencies. However, China's assertion is belied by the express text of Article 14, which sets forth binding requirements regarding subscriptions to imported newspapers and periodicals. Moreover, the binding nature of the Imported Cultural Products Measure is illustrated by the fact that it is jointly issued by the Chinese Communist Party, MOC, SARFT, GAPP, MOFCOM and the State Administration of Customs, and that it "go[es] into effect on the day [it is] published".[146] Article 18 of the Imported Cultural Products Measure offers further evidence of the binding nature of this measure, requiring the five agencies to issue implementing regulations that must be approved by the Communist Party.

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[143] U.S. Answers to the First Set of Panel Questions, paras. 269-70; U.S. Second Written Submission, paras. 198-99; U.S. Second Oral Statement, paras. 64-66; U.S. Answers to the Second Set of Panel Questions, paras. 253-57.

[144] U.S. First Written Submission, para. 386; U.S. Second Written Submission, para. 172; and U.S. Answers to the Second Set of Panel Questions, paras. 199-200.

[145] Exhibit US-10.

[146] Imported Cultural Products Measure, Article 18 (Exhibit US-10).

194. China further contends in its response to Question 272 that not all of the five agencies have issued such implementing regulations to conform to the Imported Cultural Products Measure and that those agencies enforce their existing regulations instead. However, where existing regulations are enforced that are inconsistent with the Imported Cultural Products Measure, that agency would be acting in violation of the express provisions of the binding Imported Cultural Products Measure. Thus, according to Article 18 of the Imported Cultural Products Measure, the five agencies "*shall*, *in compliance with* these Measures, draw up/improve their own concrete detailed measures for implementation, to be put into practice with the approval of the Propaganda Department [of the Communist Party]."[147] In other words, the failure to issue regulations implementing the Imported Cultural Products measure would not void, for example, the Article 14 legal requirement to examine and approve all domestic subscribers of imported newspapers and periodicals.

195. In paragraph 136 of its second written submission, however, China makes a different argument, in which it erroneously contends that while the Imported Cultural Products Measure is allegedly not directly applicable, regulations issued pursuant to this measure are directly applicable and may even be contrary to the Imported Cultural Products Measure. In other words, China argues that a measure issued by the Communist Party and five national-level agencies under the State Council that mandates implementing regulations is not applicable, but that the implementing regulations are applicable and may contradict the very measure they are intended to implement. This argument is belied by the express requirement of Article 18. Therefore, the five agencies are required to implement the Imported Cultural Products Measure through regulations that are consistent with, and not contrary to, the provisions of the Imported Cultural Products Measure.

273. At para. 159 of its second oral statement, China states that the number of distributors of imported films is not limited to two and that so far only two companies have applied and been approved. Is China saying that private wholly Chinese-owned companies, or foreign-invested companies, or other state-owned companies could apply and be approved as distributors? Please describe, with reference to the relevant legal rules, the process an applicant company would need to go through and the criteria that it would need to fulfil.

196. In contrast to China's assertion in its response to Question 273 that wholly Chinese-owned enterprises can apply to distribute imported films for theatrical release, the United States has demonstrated that no such application mechanism exists and that no such approvals have been granted.[148] Currently, imported films can be distributed by only two state-controlled

[147] Imported Cultural Products Measure, Article 18 (Exhibit US-10).

[148] U.S. Answers to the Second Set of Panel Questions, paras. 265-268.

distributors, while domestic films can be distributed by these two entities as well as the approximately 50 domestic film distributors in China.

197. In fact, China's own response to Questions 170 and 171 confirms that no application mechanism exists with respect to the distribution of imported films. Article 16 of the Provisional Film Rule states:

> The business of importing films shall be exclusively conducted by film import enterprises that are *approved* by SARFT. The distribution of imported films nationwide shall be carried out by distribution companies that are *approved* by SARFT and have the right to distribute imported films nationwide.[149]

As China has explained, the term "approved" in the first sentence of Article 16 actually means "designation" as provided for in Article 30 of the Film Regulation.[150] Therefore, the term "approved" used in the very next sentence should also be understood as "designation".

198. In its response to Question 273, China also cites Articles 36 and 37 of the Film Regulation as setting forth the application procedures for film distributors. However, these articles apply only to the distribution of *domestic* films by wholly Chinese-owned distributors. This interpretation is supported by Article 10 of the Provisional Film Rule, which elaborates on the Film Regulation's application procedures for enterprises in China (other than foreign-invested enterprises) to distribute *domestic* films. In contrast, Article 16 of the Provisional Film Rule contains no application procedures for enterprises in China to distribute *imported* films. Article III of the Film Distribution and Exhibition Rule[151] and Articles III(1) and IV(II)(1) of the Distribution and Exhibition of Domestic Films Measure[152] further confirm that imported film distributors are designated, rather than approved through an application process.

Question to Both Parties

274. With reference to the four measures challenged in the claim on sound recordings intended for electronic distribution (i.e., the Audiovisual Regulation, the Audiovisual Import Rule, the Network Music Opinions, and the Internet Culture Rule), please tell the Panel the following:

(a) What is submitted to MOC for content review? Is it the hard-copy sound recording or the digitalized version, or both?

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[149] Emphasis added.

[150] China's Answers to the Second Set of Panel Questions, Questions 170 and 171.

[151] Exhibit US-21.

[152] Exhibit US-40.

199. Despite China's contentions in response to Question 274(a), the hard-copy sound recording intended for electronic distribution must be submitted to MOC for content review. The Network Music Opinions, which were promulgated to *inter alia* "reinforce management of network music, standardize its import and promote the healthy development of the network culture industry," are based on the Internet Culture Rules.[153] The Internet Culture Rule, in turn, sets up a content review regime for "[a]udiovisual products . . .produced or reproduced by the use of certain technological means to disseminate over the Internet"[154]; under this regime, imported products that fall in this category must be content reviewed and approved by MOC while the domestic like products need only be filed with the MOC. Thus, it is clear that the content review regime set forth in these measures applies to imported hard-copy sound recordings intended for electronic distribution. In addition, this content review regime is reinforced by the content review procedures established by the Audiovisual Regulation and the Audiovisual Import Rule,[155] which China concedes in response to Question 274(a). Moreover, Article 16 of the Audiovisual Import Rule makes clear that its provisions apply to "audiovisual products imported for use in information network transmission."[156]

200. In response to Question 274(a), China begins by conceding that an imported hard-copy sound recording is subject to the content review procedures set forth in the Audiovisual Regulation and the Audiovisual Import Rule. China then notes that the Network Music Opinions only apply to sound recordings that have already been content reviewed pursuant to the Audiovisual Regulation and the Audiovisual Import Rule. China inexplicably concludes based on this that what is submitted for content review under the Network Music Opinions is *only* the digitalized content. For the reasons set forth above, China's conclusion ignores the text of the relevant measures and, therefore, does not withstand scrutiny.

(b) When the hard-copy sound recording submitted for content review by MOC, prior to, during, or after importation? What about the digitalized version?

201. In response to Question 274(b), China makes clear that hard-copy sound recordings intended for electronic distribution must be submitted to MOC for content review. Specifically, China states that "sound recordings intended for so-called electronic distribution, like any audiovisual product, have to be reviewed" before importation.[157] In other words, even under

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[153] Network Music Opinions, Preamble (Exhibit US-34).

[154] Internet Culture Rule, Article 2(2) (Exhibit US-32).

[155] U.S. First Written Submission, paras. 183-84 (the Audiovisual Regulation and the Audiovisual Import Rule require imported sound recordings to be submitted to MOC for content review while domestic sound recordings may be content-reviewed in-house by the publisher of the sound recording).

[156] Exhibit US-17.

[157] China's Answers to the Second Set of Panel Questions, Question 274(b).

China's own understanding of the relevant measures, the hard-copy sound recording is submitted for content review.

202. Moreover, by arguing that content review occurs for these products prior to importation, China is seeking to resurrect its argument that the relevant measures are border measures. For the reasons the United States has set forth previously, China's arguments in this regard do not withstand scrutiny.[158]

(c) Are the content review procedures in the Audiovisual Regulation and the Audiovisual Import Rule the same as those discussed in the context of the Trading Rights claim?

203. The United States refers the Panel to the U.S. response to Question 274(c).

[158] U.S. First Oral Statement, paras. 78-82.

TABLE OF EXHIBITS

U.S. Exhibit No.	Description
US-105	*A New Century Chinese-English Language Dictionary*, p. 823